August 1958

THE CANADIAN CHARTERED ACCOUNTANT

THE CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS

Foreign Investment in Canada

Trends in Audit Practice

Gas and Electric Utility Accounts

Accounting Procedures for the Small Store

Hospital Insurance and Company Welfare Plans

ADMINISTRATIVE ACCOUNTING: Accounting for Plant Stores
ACCOUNTING RESEARCH: Trends in Canadian Financial Reporting
TAX REVIEW: The Budget; Closely Held Corporations

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THE CANADIAN CHARTERED ACCOUNTANT

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IN THIS ISSUE

H. G. NORMAN, C.M.G., C.A. (page 132)

The most impressive feature of Canada's economic growth in the past decade has been the very high rate of investment from abroad, particularly from the United States. Certainly the country could not have done without it because Canadians, as individuals, did not have available for investment the large sums needed in order to develop the country's new industries or natural resources. Furthermore, as Henry G. Norman points out in his article "Foreign Investment in Canada", many Canadians do not appear to have been willing to take the risks inherent in primary financing but "have been satisfied in letting the non-resident put up the necessary funds". After tracing the main flow of capital contributions to Canada since the early days of the century, the author outlines some of the problems which a high rate of capital investment from abroad can create and emphasizes why Canadians should keep reasonable control of the economic development of the country.

Well-known to CCA readers as a businessman and diplomat, Mr. Norman is president of the Montreal and Canadian Stock Exchanges. A chartered accountant since 1914, he is a past president of both the Canadian and Quebec Institutes of Chartered Accountants. During World War II, he was retained in an advisory capacity by the Minister of National Defence and acted as financial adviser to the British Commonwealth Air Training Plan. He entered the Canadian diplomatic service in 1952 and was Ambassador to Venezuela for three years before being named Consul General in New York.

ST. ELMO V. SMITH, C.A. (page 125)

With the increasing complexity of business, the auditor must be constantly on the alert to improve his techniques in order to enhance the quality of his services. Some companies, says St. Elmo V. Smith in "Trends in Audit Practice", are literally risking their money on the strength of the auditor's opinion and yet, the author points out, changes in auditing practice have not received the same attention as changes in accounting principles and concepts. His article is an attempt to stimulate thinking on some of the new techniques which are available to the auditor and improve and extend his services beyond giving his professional opinion on the client's financial statements.

Mr. Smith is a partner in the Toronto office of Price Waterhouse & Co. and obtained his certificate in chartered accountancy in 1941. He is a member of the Institute of Chartered Accountants of Ontario and served for four years on the Institute's Auditing and Accounting Research Committee. In 1956 and 1957, he was a member of the Annual Conference Committee of the Canadian Institute of Chartered Accountants.

C. A. NAYLOR, F.S.A. (page 142)

The question of health is a vital one to businessmen of today and probably has been brought into sharper focus because national hospital insurance is expected to be in operation in most Canadian provinces by the beginning of 1959. Its introduction will have a far-reaching

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effect on existing welfare plans and will pose a number of important problems for those responsible for their overall administration. The reason for Carman A. Naylor's article "Government Hospital Insurance and Company Welfare Plans" results from the Editors' recognition of the fact that there could well be confusion on the part of the business executive as to the total benefits available and the costs involved under both government and private plans. Mr. Naylor outlines the Ontario plan and shows what a company can do to see that the employee is adequately covered under comprehensive major medical insurance.

The author is group actuary of the London Life Insurance Company in London, Ontario. He joined the company in 1933 and five years later became secretary and actuary of the Canadian Life Insurance Officers Association. He returned to the company in 1940 and the same year was appointed a Fellow of the Society of Actuaries.

C. A. KING, C.A. (page 148)

The small retailer is sometimes accused of being backward in his accounting methods and redeeming his inefficiencies at the expense of the buying public. It seems vital, therefore, that small retail store managements should be searching continually for the best accounting techniques suitable to their business. Competition today is very keen, far more so than has been the case for many years. This situation has prompted the Editors to start a series of articles on this important subject which should be of real use to those operating small retail businesses. Here, in "Accounting Procedures for the Small

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Store", "Cy" King, who received his certificate in chartered accountancy in 1951 and graduated with a B.Com. degree from Dalhousie University, describes the types of accounting systems suitable to the small store and the importance of monthly and annual statements. The successful small store owner nowadays must be an able administrator and the motto "You need yesterday's figures today in order to do business tomorrow" is as applicable to small storekeeping as to any other type of business.

Mr. King is with H. R. Doane & Co. of Halifax, N.S. and is a member of the Institutes of Chartered Accountants of Nova Scotia and Newfoundland.

W. C. HOWARD, C.A. (page 136)

In "Special Features of Gas and Electric Utility Accounts", Walter C. Howard examines some of the special aspects of utility accounting which, as a consequence of the expanding demand for natural gas, will result in the establishment of many new utility plants. The author deals with such subjects as overhead costs, classification of property, interest during construction and related matters. He makes special reference to depreciation and income taxes, and the recommendations contained in C.I.C.A. Research Bulletin No. 10.

Mr. Howard is a partner in the Edmonton offices of Deloitte, Plender, Haskins & Sells and a member, since 1951, of the Institute of Chartered Accountants of Alberta. He has made a close study of the accounting aspects of the province's natural gas industry and took an active part in four of the recent gas hearings before the Board of Public Utility Commissioners of Alberta.

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EDITORIAL (page 119)

This month's editorial "Changing Role of the Accountant in Industry" is contributed by an experienced business executive who takes a look at the widening scope of the accountant's function and his growing value to management. Against this background, Donald G. Scott, assistant controller of the Ford Motor Company of Canada Ltd., enlarges on the accountant's role where major financial decisions are being taken and foresees his ever-increasing importance as a participant in major business operations.

After receiving his certificate in chartered accountancy in 1935, Mr. Scott left Clarkson, Gordon & Co. to serve for a time as assistant provincial auditor for the Province of Ontario. He returned to the company with whom he articled in 1941 and, in 1947, accepted a position with Eastern Steel Products Limited, an association which lasted for seven years. In 1954, he joined Ford of Canada in his present capacity. Mr. Scott is a member of the Institute of Chartered Accountants of Ontario and a past president of the Controllers Institute of America (Toronto Control).

Forthcoming Features

TAXATION OF PARTNERSHIP INCOME

EVALUATING PUNCHED CARD INSTALLATIONS

THE SECURITIES MARKET

TRUST ADMINISTRATION AND CONTROL

ORGANIZE YOUR ANNUAL REPORT

NOTES AND COMMENTS

Forthcoming Annual Conference

Last month members received a program and registration form for the 1958 C.I.C.A. Annual Conference which will take place from September 14 to 17 at the Queen Elizabeth Hotel in Montreal. For handy reference details of the program are also published on pages 121 to 124 of this issue.

C.I.C.A. Research Committee

T. A. M. Hutchison, chairman of the C.I.C.A. Committee on Accounting and Auditing Research, announces that the following have been appointed members of the committee: I. E. Millie, Saint John; J. R. Church, Montreal; H. R. MacDonald, Toronto; G. R. Ferguson, Toronto; and F. A. Griffiths, Vancouver. J. R. Church and H. R. MacDonald will also serve on the Research Sub-Committee.

Invitation from The Netherlands

On Saturday, September 27 the Netherlands Institute of Accountants observes Accountants' Yearday 1958 at Scheveningen. The Council of the Institute have cordially invited Canadian chartered accountants who may be in Europe at that time to attend the celebration. Those who plan to do so are asked to contact the Executive Secretary of the Canadian Institute of Chartered Accountants, 69 Bloor Street East, Toronto 5, Ontario.

Consolidation Practices Surveyed

A new monograph on Canadian consolidation practices by B. J. B. Galvin, C.A. has been published by Queen's University School of Commerce and Business Administration. Professor Galvin surveyed 102 companies to obtain their experience with consolidated financial statement practices. Some aspects of his study were made possible by the Universities Trust Fund of the Institute of Chartered Accountants of Ontario. The brochure is available at $1.00 from Queen's University Press, Kingston, Ontario.

Hospital Accounting Articles

The May issue of *Canadian Hospital* contains six articles on hospital control through accounting, which have been contributed by members of the profession associated with Hudson, McMackin & Company, Moncton, N.B. We suggest that any accountant interested in this subject may wish to obtain a copy of the journal in which these articles appear. The address of *Canadian Hospital* is 280 Bloor Street West, Toronto 5, Ontario.

AICPA Annual Meeting

The 1958 annual meeting of the American Institute of Certified Public Accountants will take place from October 11 to 16 at the Hotels Sheraton-Cadillac and Statler, Detroit, Michigan.

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Accounting Hall of Fame

Harry A. Finney, author of "Principles of Accounting", Arthur B. Foye, president of the American Institute of Certified Public Accountants in 1953-54, and the late Donald P. Perry, former chairman of the Commission on Standards of Education and Experience for Certified Public Accountants, were named recently to the Accounting Hall of Fame at Ohio State University.

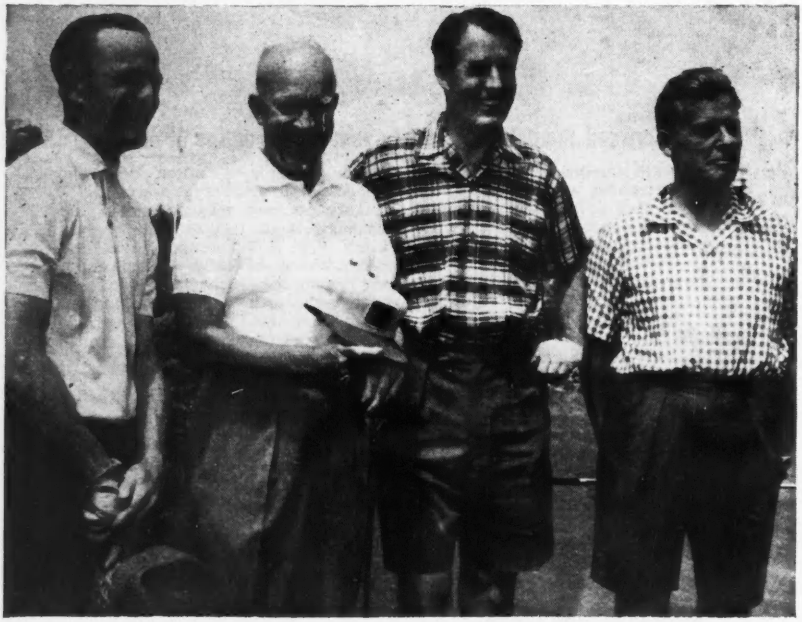
One of the charter members of the Accounting Hall of Fame, Professor William A. Paton, retired this past June from a teaching career of 44 years, most of them at the University of Michigan. Two of his books, "Essentials of Accounting" and "Advanced Accounting" are standard texts for accounting students, while among practitioners he is well known for his "Accountants' Handbook".

SICA Head

Thomas B. Milne, C.A., R.I.A., Winnipeg, has been elected president of the Society of Industrial and Cost Accountants of Canada. The society is affiliated with ten provincial societies with a total membership of 6,300 in 31 chapters.

In the News

E. L. HAMILTON, C.A., Montreal, M. S. SUTHERLAND, F.C.A., Hamilton, and THOMAS CHAMBERS, C.A., Vancouver, have been elected to the Board of Directors of Controllers Institute of America.



President Eisenhower takes time off for a round of golf during his busy 3 day visit to Ottawa last month. His partner is chartered accountant John A. Cross, (extreme left) President of the Ottawa Hunt and Golf Club. Other members of the foursome are Transport Minister Hon. George Hees and Senate Speaker Hon. Mark Drouin.

"MUNICIPAL FINANCE IN CANADA"

A brochure containing six articles on Municipal Finance which have appeared in **The Canadian Chartered Accountant.**

Each article has been written by an expert in his own subject and the series forms an up-to-date compendium of financial principles, practices and economics particularly affecting Canadian municipalities.

Topics covered are Development of Municipal Government in Canada, Municipal Budget Making and Expenditure Control, Municipal Accounting, Debenture Financing for Municipalities, Financial Control of Ontario Municipalities, Economic Factors in Municipal Government.

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Editorial

CHANGING ROLE OF THE ACCOUNTANT IN INDUSTRY

LOOKING AT the industrial scene over the last 30 years, a discerning observer will have been impressed by the rising pressures exerted on management in the continuing struggle for improved products, reduced costs and greater sales. The ultimate test in business is the ability to produce a profit. To meet this test successfully much creative effort has been expended on appraisal and reappraisal of facilities, on the search for new products and new markets, and on improvements in the efficiency of operations.

In this process there have been numerous contributors, the public accountant, the business consultant, the engineer and others. The tally would not be complete without inclusion of the accountant in industry to whom the changing situation has meant an opportunity to bring his knowledge and skill to bear in a manner not formerly permitted to him.

The accountant is certainly not a new arrival in industry, but his role has been changing and enlarging. The widening scope of his function and the increasing dependence of management upon the services he provides have been accompanied by demands for more information, to be produced earlier and more economically. Notwithstanding the changes of pace and emphasis, his standards of performance must be maintained. Even in periods of peak activity, he has to find time for reflective thinking and critical evaluation in order that his presentations and submissions will have a relevance to the subject in hand.

It was not unusual a few decades ago for the head of a business concern to feel that his own mature judgment, perhaps supplemented

by casual reference to some adviser or confidant, was sufficient justification for far-reaching decisions affecting future business action. Projections of performance in the periods ahead and estimates of cost behaviour under hypothetical conditions involved techniques which had not yet won general acceptance. In his mind there were no substitutes for sound judgment and experience. Planning, as he practised it, was a matter of intuition. While these qualities continue to be desirable in management, the complexity of modern business has brought a need for more formal and scientific methods for evaluating alternatives and reaching decisions.

It is in this area that the most significant developments affecting the accountant in industry have occurred. He has succeeded in persuading management that there are methods of forecasting the future course of business within limits of useful accuracy, that he can produce estimates of cost which are reliable, and that his advice is valuable when major capital expenditures are being considered. It would be unusual for management to proceed on almost any important venture without consulting with him. The opportunity for him to participate when major financial decisions are being taken has brought into focus the accountant's value as adviser and counsellor and given him a new sphere of usefulness and influence. His position of authority in matters of accounting policy is recognized, and it is left to him to ensure that cost and profit determinations are being made in accordance with good theory and sound practice.

The accountant in industry has much to offer in other areas as well. His broad familiarity with the whole range af activities of a particular enterprise makes him an obvious candidate for participation in planning for the future. He brings to the conference table a knowledge of current and past performance which keeps a note of realism to the fore when enthusiasm threatens to outrun discretion. Objectivity is one of his most reliable attributes. Management more than ever looks to him to measure progress when projects are undertaken and, through his reports, charts and other media of communication, expects to be kept informed.

Management shows a willingness to depend increasingly on the accountant in industry. Responsibility for initiative in demonstrating his usefulness rests with him. A pioneering spirit and persuasiveness in gaining acceptance for his services are necessary to his success. As he has displayed these traits, due recognition has come to him. This process will go on and will be accelerated as the accountant shows himself a man of broad capacity, able to think and act decisively and seasoned to the larger view by the maturity of his outlook. No longer is he a simple man of figures like his prototype of years gone by, but a qualified administrator with skills which make him a powerful contender for a post at the highest executive level.

56th C.I.C.A. Annual Conference Program

QUEEN ELIZABETH HOTEL, MONTREAL, SEPTEMBER 14-17, 1958

Monday, September 15

MORNING

Opening Ceremonies

Chairman: The President of the Quebec Institute

C.I.C.A. President's Report

James A. de Lalanne, C.A.

"The Canadian Accounting Profession and the S.E.C."

Andrew H. Barr, C.P.A.
Chief Accountant, Securities and Exchange Commission, Washington.

Annual General Meeting of Members

AFTERNOON

Public Relations Panel

Chairman: Leeds Nelson, C.A.
McDonald, Currie & Co., Montreal.

Members: Charles P. Rockwood
Director of Public Relations, The American Institute of Certified Public Accountants.
C. L. King, F.C.A.
Deloitte, Plender, Haskins & Sells, Toronto.
James J. Macdonell, F.C.A.
Price Waterhouse & Co., Montreal.
Lloyd H. Paul, C.A.
Ross, Touche & Co., Montreal.

Debate on C.A. Educational Program

Resolution: "that a greater part of the educational program for chartered accountant students should consist of lessons and material specifically designed to prepare students for positions in industry."

Chairman: Kenneth F. Byrd, C.A.
McGill University.

Debaters:

Affirmative: Marius Laliberte, C.A.
McDonald, Currie & Co., Quebec.
Robert C. Berry, C.A.
Trans-Canada Pipe Lines Limited, Toronto.

Negative: William H. Gray, C.A.
William Gray & Co., Winnipeg.
William F. Martin, F.C.A.
British Columbia Electric Company Limited, Vancouver.

Tuesday and Wednesday, September 16 and 17

N.B. The sessions planned for Tuesday and Wednesday mornings provide an opportunity for members to select one of three major topics, and pursue a brief "study course" which will combine speeches, panel discussions, and informal discussion groups extending over the two days. All Wednesday sessions will be held at the University of Montreal.

Topic No. 1 – MANAGEMENT CONTROLS

TUESDAY MORNING SESSIONS

Chairman: W. H. FLYNN, C.A.
Treasurer, Canadian Industries Limited.

Financial Management

Speakers: TREVOR F. MOORE
Vice-President, Imperial Oil Limited.
J. A. DESROCHERS, C.A.
President, Dow Brewery Limited.

Essential Elements of Controls

Speakers: R. D. ARMSTRONG, F.C.A.
Vice-President (Finance), Canadian National Railways.
ROLAND T. CHAGNON, C.A.
President, Fred A. Lallemand & Co. Limited.

WEDNESDAY MORNING SESSIONS

Simultaneous Group Discussions in English of detailed aspects as follows:

A	Inventory Controls	E	Internal Reporting
B	Cash Forecasting	F	Capital Expenditures
C	Sales Forecasting	G	Profit Measurement
D	Cost and Expense Budgets	H	Costing

Management Controls – French-Speaking Panels

Two French-speaking panels will lead discussions on a number of "Case Studies."

Chairman: GUY CHABOT, C.A.
Raymond, Chabot, Martin, Paré & Cie, Montreal.

Members: MARCEL BOYER, C.A.
Alliance Nationale, Montreal.
MARCEL ROGER LEGARE, C.A.
Davis, Bishop & Co., Montreal.

Chairman: ROGER GAUVIN, C.A.
Roger Gauvin & Cie, Montreal.

Members: JEAN-JACQUES FORTIN, C.A.
L'Ecole des Hautes Etudes Commerciales de Montréal.
GEORGES AUGUSTE PRENOVOST, C.A.
Lemay & Prénovost, Montreal.

Tuesday and Wednesday, September 16 and 17 (contd.)

Topic No. 2 – ACCOUNTING AND AUDITING RESEARCH

TUESDAY MORNING SESSIONS

The Auditor's Report

Chairman: T. A. M. Hutchison, F.C.A.
Peat, Marwick, Mitchell & Co., Toronto.

Part I–Short Papers

(a) "Consistency in Accounting Practices"
W. L. L. McDonald, F.C.A.
Price Waterhouse & Co., Toronto.

(b) "Qualifications in Reports"
Miss Gertrude Mulcahy, C.A.
The Canadian Institute of Chartered Accountants.

(c) "Reports for Unincorporated Businesses"
F. C. Burton, C.A.
Lee & Martin, Halifax.

Part II–Discussion Panels in English and French

Chairman: T. A. M. Hutchison, F.C.A.
Peat, Marwick, Mitchell & Co., Toronto.

Members: R. B. Dale-Harris, F.C.A.
McDonald, Currie & Co., Toronto.
G. P. Keeping, F.C.A.
Clarkson, Gordon & Co., Montreal.
L. G. Macpherson, F.C.A.
Queen's University, Kingston.

Chairman: Roland R. Pouliot, C.A.
Courtois, Frédette & Cie, Montreal.

Members: Francois Bastien, C.A.
Bastien & Barrière, Montreal.
Lucien Boutin, C.A.
McDonald, Currie & Co., Montreal.
Joseph Ste-Marie, C.A.
Ste-Marie & Masson, Montreal.
Clement Primeau, C.A.
Chartré, Samson, Beauvais, Bélair & Cie, Montreal.

WEDNESDAY MORNING SESSIONS

The Audit of Inventories

Chairman: D. J. Kelsey, C.A.
Helliwell, Maclachlan & Co., Vancouver.

Following an introduction by the chairman, all members will be assigned to discussion groups under group leaders, who will present brief reports when the members reassemble. Both French-speaking and English-speaking groups will be conducted.

Tuesday and Wednesday, September 16 and 17 (contd.)

Topic No. 3 – TAXATION

TUESDAY MORNING SESSIONS

"Estates Tax Act and Related Problems"

Chairman: JOHN P. KINGHORN, C.A.
Riddell, Stead, Graham & Hutchison, Montreal.

Part I — *Speaker*: H. HEWARD STIKEMAN, Q.C.
Stikeman, Elliott & Co., Montreal.

Part II — Discussion Period.

WEDNESDAY MORNING SESSIONS

"Some Aspects of Accounting and Legal Problems Confronting Foreign Companies Carrying on Business in Canada"

Chairman: JOHN P. KINGHORN, C.A.
Riddell, Stead, Graham & Hutchison, Montreal.

Part I – *Speaker*: R. DE WOLFE MACKAY, Q.C.
Duquet, MacKay, Weldon & Tetrault, Montreal.

Part II – Discussion Period.

Wednesday Afternoon, September 17

Closing Plenary Session at the University of Montreal

Chairman: JAMES A. DE LALANNE, C.A.
McDonald, Currie & Co., Montreal.

Welcome to Members: MONSIGNOR IRENEE LUSSIER, P.D.
Rector of the University of Montreal.

"Professional Life and Status"

Speaker: PETER WRIGHT, Q.C.
Wright & McTaggart, Toronto.

"Round-up Panel"

Chairman: J. R. M. WILSON, F.C.A.
Clarkson, Gordon & Co., Toronto.

SOCIAL EVENTS

Sunday evening, September 14 – Reception for members and ladies, Queen Elizabeth Hotel.

Monday, September 15 – Members Luncheon.

Monday, September 15 – Ladies Luncheon and Fashion Show, St. Helen's Island.

Monday evening, September 15 – Civic reception and buffet dinner, The Chalet, Mount Royal.

Tuesday, September 16 – Luncheon for members, to be addressed by The Hon. Maurice Duplessis, Premier of the Province of Quebec.

Tuesday afternoon, September 16 – Tour of St. Lawrence Seaway Project.

Wednesday afternoon, September 17 – Laurentian Tour for ladies, with refreshments at The Alpine Inn, St. Marguerite.

Wednesday evening, September 17 – Dinner dance, Le Grand Salon, Queen Elizabeth Hotel.

TRENDS IN AUDIT PRACTICE

St. Elmo V. Smith

CHANGES IN auditing practice do not receive the same attention as changes in accounting principles and concepts, probably because accounting changes affect financial statements directly and are therefore of wide interest to management, investors and bankers, whereas changes in audit methods are primarily only of interest to the professional auditor.

Purpose of Audits

It is perhaps useful to review the fundamental purpose of audits as a background for the trends which have developed during the last three or four decades. The protection of a company's assets from dissipation through irregularities on the part of its employees depends largely on three major factors: (1) adequate internal accounting control, which may be defined as the adoption of measures and methods to plan the allocation of duties among employees to safeguard the assets and check the general accuracy of the accounts, (2) adequate fidelity bond coverage in order that the company may recover losses suffered from defalcations and other irregularities on the part of its employees, and (3) the examination of the financial statements and accounts of the company by a professional auditor, such as a chartered accountant.

It has always been an auditor's prime responsibility to carry out an independent objective examination adequate in scope to give an opinion on his client's financial position at a given date and the results of operations for a stated period. However, with the smaller business units of earlier days and the accompanying smaller accounting staffs, the auditor frequently had to carry out extensive tests of the detailed transactions of a business in order to ascertain that the accounting records properly reflected the business operations and furnished information on which he could base a sound opinion as to the fairness of the financial statements. Further, the general public, as distinct from the informed business community, felt that the auditor's main function was detection of fraud and irregularities since the average individual's knowledge of auditors had to do with, say, bank inspections in small communities and municipal audits. Thus the auditor's program was somewhat heavily weighted towards the detection of fraud, irregularities and errors. This was partially

because of the public conception of an auditor's duties and partially because in many instances the client's staff was not adequate in either knowledge or numbers to detect such irregularities or produce accurate accounts.

Changes in Audit Emphasis

During the past 40 years there have been many factors contributing to the change in audit emphasis. In the earlier period the Canadian economy depended largely on agricultural products and extraction of natural resources whereas now we have highly industrialized communities contributing substantially to the nation's wealth. With the tremendous relative growth in number and size of commercial and industrial business units and the vast number of transactions to be recorded, there has, of course, been an accompanying increase in accounting staffs. This has made it possible for effective systems of internal control to be developed in medium and larger businesses.

In earlier days many businesses were controlled by sole owners or family groups who had intimate knowledge of their business affairs and were therefore in a position to know generally what the operating results of the company should be and depended in part on the auditor to detect minor irregularities. With the growth in the size of business units there has developed a management group, frequently with small shareholdings, who run the company's affairs on behalf of a large body of shareholders who have no intimate knowledge of the company's day-to-day operations and what financial results should be achieved. As a result, it is increasingly important to have an independent examination of the financial statements of a company for presentation to the shareholders since the management group must of necessity be subjective in its approach rather than objective.

Another relatively modern condition is the high rate of corporate income tax which makes it imperative for the annual income of a corporation to be determined with a reasonable degree of accuracy. Canadian auditing and accounting practices have also been influenced by those followed in the United States and by such regulatory bodies as the Securities and Exchange Commission, Washington.

Auditor's Responsibility

For these reasons, it is now generally accepted that the auditor's principal responsibility is to make an independent examination of a company's financial statements in order that he may report as to whether or not in his opinion they fairly present the company's financial position at a given date and the results of its operations for a given period. It is recognized that an auditor's examination of financial statements may possibly detect minor cases of fraud and error but that he can only be expected to detect such conditions if they are of sufficient magnitude to impair a company's financial position or distort earnings for an accounting period as compared with previous periods. It is the prime responsibility of accounting officials of the company to find errors and irregularities through arranging the accounting system so as to lead to an early detection of any such conditions. Thus there has been a marked shift in emphasis from earlier days and now an adequate system of internal accounting control and proper fidelity bond coverage are

the primary protection against errors and irregularities with an audit by a chartered accountant providing the broad overall protection.

Judging Internal Control

As a result of the factors referred to above, there has been a significant change in audit practice in that the auditor's program has been directed more and more to establishing that the client's system of internal control is functioning properly and should produce accurate results rather than carrying out extensive tests of, say, three, four, six or more months' transactions. In medium-sized and large businesses this program has been designed towards ascertaining the nature of the internal control, and seeing that it is functioning through carrying out limited tests of the detailed transactions of the company which may cover only selected transactions within one month. It is sometimes stated that it would be economically impossible for the auditor to carry out the extensive tests that were formerly made, but it would seem that economy is really not the fundamental factor in this change. Rather, because of the increase in the size of business units and the additional accounting staff required to deal with the vast increase in transactions, it is possible to improve the company's internal control to a point where it is no longer necessary for the auditor to carry out the extensive tests used in the past.

Judgment is one of the attributes of a profession. A professional auditor must always use his best judgment in determining what steps or techniques he should take in order to place himself in a position to form an opinion on the fairness of the client's financial statements. Thus, if the internal control in a client's office is not adequate, an auditor must of necessity do sufficient work to satisfy himself that the accounting records properly record the transactions of the company despite any question of cost or economics, and in past years this often led to extensive tests of detailed transactions.

New Audit Trends

During the last 10 or 15 years, two audit procedures have been introduced on an increasing scale in Canadian practice. These steps are the confirmation of accounts receivable balances by direct correspondence with the debtors and the observation or test checking of physical inventories. As yet they have not been laid down as prescribed procedures by the Committee on Accounting and Auditing Research of the Canadian Institute of Chartered Accountants, but from various surveys it is evident that they are being carried out by increasing numbers of Canadian chartered accountants. In view of the fact that more and more members of the profession are carrying out these steps it is likely that the Research Committee will, in due course, recommend them as procedures to be carried out on all examinations. These two audit procedures are undoubtedly a development of the further emphasis on the review of internal control since they both serve to check the effectiveness with which a client's laid down procedures are being carried out in practice.

Another of the trends in recent years has been the shifting of work from the year-end date to interim periods in advance of the year-end. This shift undoubtedly arose from a variety of reasons, two of which were the serious staff difficulties encount-

ered in most auditing firms during the war years when it became impossible to carry out all audit work at the year-end and, secondly, the recognition that where adequate internal control was functioning it could be reviewed and checked at other than year-end dates. The days when hordes of juniors and temporary staff descended on a client shortly after the year-end to carry out the majority of the work on inventories, accounts receivable and cash, are largely past except for smaller clients where the internal control is not sufficiently strong and where it is uneconomical to make more than one visit during the year. As a result, physical inventory taking and the pricing and comparison of inventory values with book values is usually carried out two or three months before the year-end; accounts receivable are circularized, tested and reviewed for doubtful account provisions at an interim month-end during the same period. A substantial amount of work on bank transactions is also completed in advance of the year-end. This trend is desirable from the standpoint of the client's staff in that it removes some of the pressure formerly associated with the preparation of year-end financial statements and the auditor's visit. It also assists the auditor in levelling out his work over the course of the year and thus probably tends to result in a more satisfactory examination.

As a result of the increasing emphasis on the client's responsibility for developing adequate accounting systems, there has been a definite trend towards visiting fewer branches of multi-branch companies. Twenty years ago it was the exception rather than the rule not to visit a branch of any consequence whereas now it is common practice to examine the accounts maintained at branches on a rotating basis so that perhaps important branches are visited every other year and less important branches every two or more years.

Although internal audit staffs have been employed by large organizations such as the Canadian chartered banks for many years, more and more industrial concerns now have internal auditors. They work in close collaboration with the shareholders' auditor and are part of the overall system of internal control which provides a check on the proper recording of business transactions.

New Avenues of Approach

Several problems and some new avenues of approach are presently facing the auditor. One possible approach, particularly for larger organizations for which the same auditor has been examining the accounts for many years, is that of a more or less continual examination of a company's accounts. Reports on financial statements are prepared annually, but the work on certain balance sheet items, such as cash, accounts receivable, inventories and property accounts is carried out on a rotating basis, say, once every two or three years. This would appear to be a logical sequence of the trend towards reliance on a company's internal control to produce accurate financial statements and somewhat analogous to the rotation of work at branches which is now generally accepted. An article expounding the various features of this approach is included in the April 1956 *Journal of Accountancy*.[1]

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[1] "A Suggested Change in Examination Approach" by A. Carl Tietjen.

Another possible avenue of approach to modern auditing is the use of statistical methods in sampling and test checking. Although these have not had any wide acceptance as yet, there are undoubtedly some fields for which statistical methods might be suitable and efficient, particularly where the volume of transactions is large, such as testing sales, invoicing, payrolls, stores inventory records and perhaps circularization of accounts receivable. Details of the problems involved in accepting this method are set out in an article in the December 1956 issue of *The Canadian Chartered Accountant.*[2]

Auditing E.D.P. Records

One of the frequent questions a chartered accountant faces these days is "How do you audit results produced by electronic data processing methods?" In this connection it must be recognized that certainly at the present only large organizations can afford the cost or make economic use of electronic data processing installations. As stated before, the prime responsibility for maintaining proper accounting records in such organizations rests with the accounting officials and they have to be satisfied as to the reliability of the data processing methods before they will be accepted. If this group can be satisfied it is probable that similar information is available to satisfy the auditor although it may involve a closer association with current data being processed rather than checking detailed transactions five or six months after the event. It should also be understood that certain controls are built into electronic data processing machines by the manufacturer and that other accounting controls can be set up to check on the results produced by the system. For instance, in its present stage electronic data processing systems may well provide for an operating group originating the original source documents, a data processing group which, as a service centre, processes information obtained from other departments, and a custodian group handling treasury functions. It is also possible to maintain manual controls outside the service centre. For example, in respect of payrolls, control totals of numbers of employees can be maintained and changes in gross pay from week to week for salaried employees can be used to reconcile changes in gross payrolls between pay periods.

In considering the electronic data processing service centre itself we are interested in obtaining assurance that there are enough controls in operation to catch mistakes if the machine starts producing incorrect information or if the program is set up incorrectly either through deliberate or innocent error. In this regard the auditor should know about the controls available in an electronic computer and enquire from his client that none has been deleted without good reason. He should also know about other program checks and controls available and determine that they are being properly used. This will involve some degree of technical training but will not require a detailed knowledge of the equipment or its processes. It will, of course, be essential for him to review the division of duties and the segregation of authority in the service centre.

With regard to carrying out our normal audit procedures it appears that his ability to audit specific items

[2] "Statistical Theory in Test Checking" by E. L. Pursey.

in the balance sheet will be less affected by the conversion to electronic equipment than his ability to examine selected detail transactions to establish the integrity of the system of internal control. He can still carry out our circularization of receivables and pricing of inventories, but some problems may arise, say, when he wants to test a payroll distribution. However, the problem of tracing transactions back to original documents is not as serious as one might think at this stage. Some of the problems raised in informal discussions on this topic are based on the unrealistic assumption that visible records will disappear and that a "magic brain" makes all decisions and keeps all records.

It presently appears from a review of literature by experts in the field that electronic data processing may be expected to advance through the following three stages:

1. Visible source material will be prepared by the same methods as before and converted to electronic machine information prior to processing (e.g. employee's clock card from which paper tape is subsequently prepared).
2. Original source material, both visible and electronic machine information, will be prepared simultaneously (e.g. paper tape is produced at the same time as clock card is punched).
3. The source data will be electronic machine information only (e.g. the use of employees' keys to punch a time clock, no visible time card being produced).

As we are predominantly in stage one in respect of present installations it would appear that we will be able to evolve along with the changes rather than making any revolutionary changes in our basic approach or thinking.[3]

It is impossible to lay down prescribed methods and procedures for carrying out all audits since a sound and enlightened audit must be carried out by a skilled professional auditor with a basic background of auditing practice and judgment formed through years of experience. This is one of the reasons why auditing literature outside of textbooks has been either of a very general nature or a very specific nature covering certain limited examples, such as the case studies released over the past few years by the American Institute of Certified Public Accountants.

All of the foregoing trends have developed or will develop gradually as deemed appropriate in the judgment of the professional auditor.

Skilled Assistance Required

One of the more important features of the new trends has been the necessity of having highly trained and skilled senior and junior assistants in order to carry out audits which require the continual exercise of judgment throughout the course of an examination as compared with earlier years when extensive tests of several

[3] Information on auditing records produced by electronic data processing systems has been obtained from the brochure "The Auditor Encounters Electronic Data Processing" prepared by Price Waterhouse & Co. for International Business Machines Corporation. Further information on the subject is contained in "Integrated and Electronic Data Processing in Canada" published by the Canadian Institute of Chartered Accountants.

months' transactions were carried out, sometimes in a rather routine manner. Judgment, of course, is not a characteristic that comes automatically with any college degree or other training but depends on the basic intelligence of the individual, the recognition of mistakes of earlier poor judgment and the gradual maturity to form sound decisions based on past experience and training. Modern auditing practice requires the best trained individuals, and more and more university graduates are going into the profession. With the instruction they received through their various courses and their training in a chartered accountant's office, they will undoubtedly provide the necessary leadership for the profession in the future.

With the increasing complexity of business, governmental regulation of various enterprises, and the speed up in communications, the auditor today has an increasingly important part to play and must be constantly alert to improve his methods, techniques and general attitude in order to carry out effective examinations of financial statements and render independent objective opinions useful to all elements of the business community, some of whom are literally risking their money on the strength of the auditor's opinion.

"To Err is (Almost) Human"

From time to time we receive literature extolling the virtues of computing machines. About their many virtues there can be no doubt; in fact such inhuman accuracy is almost a little terrifying. It comes, therefore, as a refreshing change to read a report in the daily press of a machine which — we almost said "who" — made a mistake.

This machine, which belongs to an Area Gas Board in England, is apparently in the habit of producing occasional freak figures, presumably as a result of the Board's decision "to get the advantages of mechanization without spending a great deal of money on an elaborate machine", as the Parliamentary Secretary to the Ministry of Power delicately put it. Manual checks are therefore made, but for once there was an oversight and a local butcher was sent a gas account for £999,999, 19s. 11d. The idea of paying exactly a penny less than a million pounds for one's gas bill seems like a bit out of the type of fairy tale that tells of a king's ransom that is to be paid in a year and a day — especially as the butcher who received the bill had burned no gas at all.

—*The Accountants' Magazine*, April 1958

Foreign Investment in Canada

HENRY G. NORMAN

THE IMPORTANCE of foreign capital to Canadian development has been an outstanding characteristic of our country's economic history and will undoubtedly continue to have a definite influence on its future, both from an economic and political viewpoint.

In the early days of our development, when we were not yet ranked as an industrial nation, the major investments of capital were largely in railways and other public utilities, and in spheres of social capital financed by government borrowing. The flow of the more important capital contributions fifty years ago corresponded with the direction of Canada's political allegiance, and such borrowing from the United Kingdom was in the main subject to repayment. In some cases, it took the form of funded debt guaranteed by the Government of Canada.

With changing times and, more particularly, as a result of two world wars, our expansion was of necessity speeded up in order that we could play our part both in manpower, food supplies, and manufactured products for munitions of war. The availability of funds from Great Britain being materially reduced, it was only natural that we turned to the United States for financial and technological aid to help us carry out the development and expansion of our economy.

When American capital began to flow into Canada in substantial amounts, it was not in the form of loans and borrowed money, but through direct investments in Canada which, in many cases, carried with it ownership and control. Here, perhaps, we touch the real source of uneasiness, in the fact that we have no precedent for our present situation.

Before World War I

In 1900 foreign investments in Canada had a value of some $1¼ billion. By 1957 they had exceeded $15 billion. This growth was somewhat irregular, being most pronounced in the decade prior to World War I, the inter-war period up to 1930 and the recent post-war period. Reductions occurred during the mid-thirties, with further significant withdrawals of capital forced upon the British to assist them in their financial requirements during World War II.

In the period preceding World War I, the expansion in wheat production, lumbering and railway building was the core of economic development, and as the London capital market was the principal available source of the capital needed, there was a wave of capital inflow from the United Kingdom. It was in this era that the largest part of Canada's indebtedness to the United Kingdom was incurred, estimated at $1 billion compared with $168 million for that of the United States.

The termination of this period is marked by the changes brought about

by the World War I. The demands of the allied governments led to large current surpluses in Canada and the direction of development changed with inflows of capital being largely confined to new issues of government bonds in the United States. The increase in United States investments to nearly $1-2/3 billion during the four war years was as large as the increase in the period from 1900 to 1914 and contrasts with the beginning of a decline in British investments in Canada.

Between the Wars

A new period of even greater growth in United States investments occurred following World War I. In contrast to the period before the war, capital for industrial expansion, with much of it in the form of direct investment, played a larger role. The major source of foreign capital in Canada shifted to the United States, whose estimated share was then over $3 billion.

The decade of the 1930's was a period of generally low investment activity in Canada and this was a time when British and United States investments in Canada combined were reduced from $7.4 billion to $6.6 billion. The two principal ways in which reductions occurred were through repatriation of Canadian securities owned abroad and through withdrawals of capital invested in direct investments. The repatriation mainly occurred by redemption of bond issues owned abroad at a time when new issues floated abroad, for other purposes than refinancing, were relatively light compared with the extent of new borrowing by this means in the preceding decade. The withdrawal of capital invested in branches and subsidiaries probably was a reflection of the reduced scale of business activity and the absence of any general expansion in properties. In contrast to the decline in British and United States investments, there was a rise in investments by other countries. This latter was concentrated in the years immediately before World War II and was mainly European capital in search of security.

During World War II the most outstanding change in external investments in Canada was the substantial reduction in British investments, from $2.5 billion to $1.7 billion, which mainly occurred from official repatriation operations connected with wartime financial arrangements. There was during the period, however, a net increase in total external investments in Canada as investments by the United States rose appreciably, and there was a continued growth in European and other foreign capital in Canada. The rise in United States investments was in both direct and portfolio investments. Canada's balance of indebtedness was sharply reduced in this period by a substantial growth in Canadian assets abroad through Canadian government loans and an accumulation of official reserves.

Post-World War II

Following World War II, there was another period of intensive growth in Canada in which non-resident capital played an important part as reflected in a sharp rise in non-resident investments in Canadian industry. Most of this rise occurred in the years since 1948. While, in the aggregate, non-resident resources contributed a smaller portion than in other periods of increased investment as a whole, the contributions of non-resident capital were of major proportions, par-

ticularly in the sphere of industrial and resource development.

In this latter period, investment by non-residents has doubled itself from $7 billion to over $15 billion. But the significant aspect of this rapid increase is the concentration in direct investments in Canadian industry which carry with them control and ownership as well as policy direction having its effects on Canada's international trade; this has been particularly evident in the industrial field where large aggregations of capital are essential. Manufacturing, mining and petroleum are the areas of investment where non-resident controlled companies represent more than half of the total capital invested. In manufacturing alone, excluding petroleum refining, the non-resident controlled portion is nearly 50%, in petroleum 70%, and in other mining approximately 55%. Most of these concerns are controlled in the United States.

The size of this capital movement and its rate of acceleration have brought about an intangible sense of disquiet in Canada, giving rise to the question as to what price we are paying as a nation for our rapid development. But where would Canada be today, if we had not had this outside capital participation?

It is only reasonable that foreign investors lay down policy for the Canadian company or subsidiary that they control, but in laying down a policy more thought might well be given as to the effect that it might have on the Canadian economy. A foreign investor who has taken risks inherent in any investment is entitled to share any monetary benefits so derived, but it should not be forgotten that he has responsibilities to Canada as a whole, over and above that of his controlled company. It would appear difficult to lay down any formula to define this responsibility, but foreign controlling interests might well resolve the problem in not only having Canadian management and directorate, but by taking into consideration in their overall planning the best interests of the Canadian people and its economy as a whole.

Preponderance of American Capital

Our country has always depended, to some degree, on foreign capital for its development, and large-scale American participation is nothing new as it started to outstrip that of the United Kingdom some 30 years ago. It must be admitted, however, that American investment in the two decades prior to 1945 increased by less than $2 billion, whereas in the years following World War II it has grown by over $7 billion. Consequently, of over $15 billion dollar non-resident investment in Canada today, over $11½ billion is held in the United States, $2½ billion in the United Kingdom, and the remainder in other countries. Direct investment from the United States is estimated at $7½ billion (64%) as opposed to $4 billion (36%) of portfolio investment. It is interesting to note that this percentage ratio is just about the reverse of that for the United Kingdom and other non-resident countries, where portfolio investment accounts for approximately 62% of their holdings and direct investment the remaining 38%.

This preponderant share of American capital invested in Canada is significant in itself, but in comparison with Canada's national wealth estimated at over $200 billion, it is a very small percentage. The rapid development in the last decade, undoubtedly accelerated as a result of

foreign investment, has created new and wider opportunities for Canadians to play their part in filling the needs for management skills. We should also remember that the whole development of non-resident investment and its consequences have taken place in an expanding Canadian economy. The financial and technological aid of the United States has been one of the prime factors in our country's expansion, but it is still only a part of a much larger scene of affairs controlled, financed and directed by Canadians.

We should be thankful to our neighbours for the part they have played in the development of our resources for without their investment participation, Canada might not have attained its present enviable position as one of the leading nations of the world.

This is not a time for criticizing the manner in which the development of our country has taken place, the means used for such development, nor the rewards that the providing risk moneys have reaped for those who took the risks. Rather, it is time for us all to sit down, not only at political and governmental levels, but as individuals, to appraise our outlook for the future and decide what course of action should now be taken.

Finance the Keystone to Growth

Finance is the keystone of starting an industry, and involves not only primary financing, but secondary financing as well.

A primary market is essentially a financing market. It is the market which promoters and financiers use to provide risk money for new enterprises involving buildings, equipment, exploration, development and similar purposes. A secondary market is the only type of market maintained by most stock exchanges. On this market are securities of relatively proven companies that have already been through primary financing markets.

Many Canadians appear to have been unwilling to take the risk inherent in primary financing and to have let the other fellow (non-residents) put up the necessary funds. In this type of financing, if the industry is not successful, the financier must take the consequences. If it is successful, he then reaps the benefits and profits. There are risks involved in any enterprise, but the people of Canada have the funds, the technical know-how and the manpower to bring such enterprise to fruition. We may not as individuals have access to the larger sums needed to develop new industries or our natural resources, but with sound leadership the financial resources of the mass of the people can and must be directed into these channels if we are to keep in Canada a reasonable control. Investment is one of the true democratic rights that we all enjoy, and with it goes the right to share in a company's financial and capital growth, as well as the power to vote on its directorship and policy. We, as Canadians, must take upon ourselves these responsibilities by investment in Canada, be it primary or secondary, and thus ensure to Canada control of its own future.

Special Features of Gas and Electric Utility Accounts

WALTER C. HOWARD

In 1951 there were 252,000 natural gas customers in Canada. By 1957 this figure had increased to 609,000. The construction of pipelines carrying natural gas from Alberta to the east and west will accelerate the rate of this expansion and bring about the establishment of many new utility plants. It may be well, therefore, to consider some of the special features of utility accounting and consequently the audit procedures of these companies. The following comments are intended to apply mainly to regulated gas and electric utilities of the free enterprise type.

In Canada there is no uniform system of accounting for regulated utilities. Each province has different legislation and this often imposes problems on companies operating in more than one province.

The purpose of public utility regulation is to limit the return to the proprietors to a reasonable amount because usually it is more economical for only one utility to operate in a given area and therefore such a utility enjoys a monopoly. This is accomplished through the power of the regulatory body to set the rates which the utility may charge for its service. The method most often used by commissions consists of two basic factors. These are the "rate base" (being the assets used in providing the service plus working capital) and a percentage allowed on the rate base as a fair rate of return.

Regulation makes utility accounting unique in that the selling price of the service depends to a large degree on the value of the company's fixed assets. In general, it will also be found that the investment in utility plant is exceptionally large in relation to revenue and return. The accounting for utility plant therefore may be said to form the salient feature of a utility audit.

The external auditor should first review the accounting policies of the company to determine whether or not accepted accounting principles are being followed. There are important common characteristics in all regulated industries, and in order to assist in the review of the accounting policies of the utility, consideration should be given to certain special problems arising out of conditions imposed by regulation. Some of these are as follows:

Classification of Property

Property must be recorded at its "original cost" (that is, the cost to

the person first devoting it to public service) and separated into functional classifications as, for example, transmission and distribution systems. Any excess of cost to the present owner of the property over the depreciated cost of such property to the original owner is normally carried in a "plant acquisition adjustments" account. Any subsequent write-ups of the property are also carried in this account. It would appear to be desirable to show adjustment accounts of this nature separately on the balance sheet.

General Overhead Costs

Most of the difficulties surrounding the treatment of overhead costs arise from the necessity of separating such costs between the utility plant and the operating expenses, and in the subsequent distribution of capital costs to the various classifications of plant. This is particularly true where a utility company undertakes a large portion of its own construction. In determining the amount of overhead costs to be capitalized most uniform systems of accounts allow the capitalization of actual and reasonable overhead costs. The burden of proof in establishing the validity of these costs for rate-base purposes lies with the utility.

Interest During Construction

Interest during construction in a regulated utility has always been recognized as a proper charge to the cost of construction, but a great deal of controversy has centred around the amount of the allowance. There is plenty of room for difference of opinion as to the period of construction and the question of operation prior to completion of the entire project, but the main argument has been over the assumed rate of interest, usually taking into consideration the rate of interest on equity funds as well as on borrowed funds.

Entries giving effect to capitalized interest for equity funds are rarely encountered in ordinary commercial enterprises, although several of the provincial Companies Acts sanction payment of dividends during construction and charging this amount, together with interest on borrowed funds, to cost of construction (B.C. Act, chapter 42; Alberta Act, section 102). However, in accounting for regulated industry, the capitalization of interest during construction (including interest on equity funds) is the accepted procedure, the credit usually appearing in the income account. In the United States all the uniform systems of accounts under the Federal Power Commission set forth this procedure as the one which must be used.

On page 44 of the "Uniform System for Natural Gas Companies" it is stated that "interest during construction includes a net cost of borrowed funds used for construction purposes and a reasonable rate upon the utility's own funds when so used". In a 1952 case, the Federal Power Commission interpreted the above as follows:

> We have generally allowed the actual cost of borrowed funds and a 6% rate of interest on corporate funds used for construction purposes. It has been our practice to refuse to allow the capitalization of interest during construction at rates which would result in a high profit during construction for the allowance is not for the purpose of providing the company with a fair rate of return before operations begin.

A review of a number of recent Canadian utility financial statements

showed that interest rates varying from 4½% to 7% were being used. This variation would indicate that different principles were being applied in arriving at the composite rate for interest during construction. The issue appears to lie in the interpretation of the purposes of the allowance.

Regulatory authorities tend to approach the problem from the "cost of money" concept (i.e. a reimbursement of actual cost of money needed to finance construction, this usually being a combination of the interest cost of borrowed funds and an amount for equity cost based on the fair rate of return), whereas the electric and gas utility industries usually adopt the view that the purpose is to record the investors' claims to recovery of a return for the economic sacrifice and risk during the construction period. Those adopting the latter view believe that a regulated utility is entitled to a fair rate of return on its investment and that the investment includes that portion represented by utility plant under construction. In this connection it is interesting to note that the Public Utilities Commission of British Columbia recently approved a rate of 6½%, equivalent to the fair rate of return allowed to the company in question by that commission.

Depreciation and Income Taxes

Because of the emphasis over the years which has been placed on the valuation of fixed assets for rate base purposes, depreciation has likewise received its share of attention. With the utility cost concept now firmly established, most Canadian utility companies are using straight line or reducing balance depreciation methods rather than retirement accounting procedures.

However, an entirely new field of controversy has been opened with the repeal in 1954 of regulation 1100 (4) of the Income Tax Act (limiting capital cost allowances claimed for tax purposes to that shown in the company's books). Since then most utility companies have claimed for federal income tax purposes the maximum cost allowance permitted under the Income Tax Act, but have continued to record in their books the engineering or normal depreciation. If the company followed the preferred treatment set forth in paragraph 10 of C.I.C.A. Accounting Research Bulletin No. 10[1], a difficult problem might arise in determining the rate base and the net utility income.

In commenting on the preferred method outlined in Bulletin No. 10 in a 1956 rate hearing before the Board of Public Utility Commissioners of Alberta, the late R. Winslow Hamilton, F.C.A. stated:

> I find no quarrel with that authority whatsoever. There is nothing to stop this or any other company making suitable provision on its balance sheet so that the shareholders may be informed of that situation. However, the necessity or the wisdom of making that sort of clarification on the balance sheet has much more force in a non-utility company than it has in a utility company because, if income tax is to be allowed as a component of the service rate, then income tax that is to be paid in the future is passed on to the consumer in any event. Perhaps I should clarify that. In a manufacturing concern, or any other non-utility business, the general situation is that you make what profit you can, and out of

[1] Paragraphs 9, 10 and 11 of Bulletin No. 10 issued by the Committee on Accounting and Auditing Research of the Canadian Institute of Chartered Accountants are as follows:

"9. It has been suggested that, in the

those profits you pay your tax; the question, of course, in the utility field is somewhat different. Income tax is not paid out of your earnings but is an element under normal regulatory practice of the costs which are passed on to the consumers.

The company, in its submission, had followed the procedure set forth in paragraph 10 of Bulletin No. 10. In its decision, the Alberta Board of Public Utility Commissioners stated:

> The effect of adopting the company's plan would be to compel the consumers to contribute to the capital of the company, whereas the company itself should provide the capital on which the consumers pay a rate of return. After giving the problem serious consideration, the Board has come to the conclusion that it should not adopt the treatment of income tax advanced by the company. It will allow the company to take income tax on the basis of the tax actually paid or payable.

It would appear that the real issue in determining whether paragraph 9 or paragraph 10[1] of the bulletin applies might be whether the tax saving is a temporary or a permanent one, and this in turn is dependent upon whether future replacements of depreciable assets may be expected to equal or exceed retirements. With the prospect of Canada's continued expansion, together with the likelihood that the price level will continue to increase, it would appear that insofar as regulated utilities are concerned, paragraph 9 of Bulletin No. 10 may well be the preferred treatment.

Before leaving the question of Bulletin No. 10, comments made by the panel discussing "Accounting Problems in the Oil Industry" at the 1957 C.I.C.A. convention have a bearing on those gas utilities owning their own wells. This panel's discussion revealed that paragraph 9 as well as paragraph 10 of the bulletin were rarely used in the oil and gas industry when dealing with the writing-off of well development costs.

Customers' Advances and Contributions for Construction

In order to obtain service from the utility in situations where it would otherwise be uneconomic, customers are often called upon to contribute towards the cost of the necessary extension. These advances may or may not be refundable in whole or in part, depending upon the particular contract provisions. Sometimes these advances are viewed as being a compensation for estimated operating de-

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circumstances, the net profit for the year may be reported as the amount determined after charging as income tax the amount actually payable in respect of taxable income for the year, provided that the effect of the reduction of taxes payable on the net profit for the year and the net accumulation of such amounts are set out in an explanatory note on the financial statements.

"10. On the other hand, it has been suggested that a material reduction of current income taxes, resulting from claiming capital cost allowances in excess of recorded depreciation, should be treated as applicable to those future years in which depreciation corresponding to the excess is charged in the accounts rather than reflecting such reduction in the reported net profit of the current year.

"11. While the procedure outlined in paragraph 9 sets out the minimum essential information, the committee believes that in most circumstances, it is desirable to report the net profit as determined by following the procedure suggested in paragraph 10. This procedure conforms to the principle of matching costs and revenues and avoids any uncertainty as to whether a note, such as is suggested in paragraph 9, is merely an explanation of the basis on which the net profit has been determined or constitutes an adjustment of the reported net profit."

ficits which the utility will have to bear until such time as an adequate return can be realized from the investment, in which case these payments by customers may be treated as non-refundable prepaid revenue. In any case, the accounting disposition of these payments should be deferred until all liabilities to the customer have been discharged.

Unless the regulatory body has set down the accounting procedure, there may exist considerable uncertainty as to the proper disposition of the credit in the "contributions in aid of construction" account. Some U.S. commissions have ruled that these contributions be credited to the plant accounts, thus recording the cost of the utility plant at its net cost. Most commissions in Canada have as yet made no ruling on this matter, and a review of 1956 utility financial statements has shown large credits on the liabilities side of the balance sheet. It would appear that these credits should not be transferred to such accounts as surplus or reserve accounts without the commission's approval.

Since the advances were not made for the purpose of enabling the utility company to charge higher rates, most commissions have ruled that in establishing the rate base these advances should be deducted. However, since title to the extension rests with the utility company, and since the asset will have to be replaced eventually by the utility, it has sometimes been held that depreciation on these particular assets is a proper charge to be used in determining rates.

Joint Costs

In utility accounting, the concept of the accounting entity is recognized to the point that even a department or a branch of a utility company may be classed as a separate utility. This introduces the problem of allocating joint costs since many utility costs apply to all the services rendered. In determining the basis to be used in the allocation of costs it will rarely be found that a single variable will properly reflect the correct value of property used or expense devoted to the division, class or service. Variables such as use, time spent, kilowatt hour or M.C.F. delivered, or number of customers may have to be given consideration. Most uniform systems of accounts provide for "clearing accounts" to facilitate the handling of these costs. A review of the operating and construction budgets of the company may assist the accountant or auditor in difficult problems of cost allocation.

Revenue and Trade Receivables

A special feature of utility accounting, brought about more by the nature of the business than the fact of regulation, is the accounting for revenue and trade receivables. These two items are so inter-related that they are usually treated as a unit in considering accounting and auditing procedures.

In billing their customers, practically all gas and electric utilities use what is known as "cycle billing". The billing is usually done from a central billing office, the customer accounts being divided (with separate ledgers and control accounts) into districts or divisions of from 200 to 500 customers. The billings are made as nearly as possible on the same date each month. Trial balances (known as "cycle balances") are taken off immediately before the monthly billings ("cycle date") and are posted and

balanced to the control account. At the month-end no balancing of detailed lists of customer receivables are made with control accounts except for those districts where the end of the month coincides with the "cycle date". The unbilled electric and gas revenue is frequently not accrued since the condition is practically the same at the beginning and end of the accounting period.

The great volume of accounting detail usually makes it impracticable for the auditor to prove with the control account at any specific time the details, for example, of 50,000 customer accounts receivable. The auditor therefore relies on audit procedures used in evaluating the internal control to provide a check on utility revenue billings and the reliability of the customer accounts receivable. An important check on this feature of internal control is the confirmation of customer accounts by direct correspondence. Statement No. 14 issued by the Committee on Auditing Procedure of the American Institute of Certified Public Accountants in December 1942 on this same subject concluded by stating: "Such a test confirmation is desirable even in cases in which test confirmations may be made by internal auditors employed by the utility."

General

One aspect of utility accounting which is of considerable interest and perhaps important to the accountant and auditor is what has been described as "the finality of past accounting". Many United States commissions and at least one Canadian commission appear to have taken the stand that once an accounting decision has been made it cannot be adjusted retroactively for rate purposes, e.g. plant accounts may not be adjusted upward for failure to charge asset costs in the past. This rule, of course, does not prevent the commission from retroactive deductions from utility plant in connection with improperly charged overhead, assets not used, etc. Since utilities are usually precluded by commissions from recovering past losses out of current and future charges to consumers, the external auditor should not be surprised to find that in certain situations utility management often consider the normal conservatism inherent in accounting principles to be inapplicable. For example, if doubt exists as to whether certain charges are capital or expense and actual capital items are charged to expense in years when the company was not making its allowed return, these costs may never be recovered from the consumers to the ultimate detriment of the company and its shareholders. The recording of depreciation in excess of normal (e.g. maximum allowable under Income Tax Act) in years of inadequate return may also have the same effect.

Professional accountants are by training and experience well versed in the art of evaluating the effect of accounting entries on the shareholders' interest and the omnipresent Minister of National Revenue. In utility accounting they will be called upon to consider the addition of a third dimension to their thinking, i.e. the requirements of the regulatory body. In other words, the utility accountant must often try to serve not two but three masters and all at the same time.

Government Hospital Insurance and Company Welfare Plans

C. A. NAYLOR, F.S.A.

GOVERNMENT HOSPITAL insurance plans have been in effect for a number of years in a few Canadian provinces, notably British Columbia and Saskatchewan, and there has been little scope for the development of private plans in these provinces. In most Canadian provinces, however, private hospital insurance plans have had a widespread growth in recent years to the point where a very high proportion of employed groups have some form of hospital insurance.

The introduction of government hospital insurance in many of these provinces in 1958 will have a far-reaching effect on existing welfare plans and will pose a number of important problems for those responsible for these plans. Since Ontario is the first province to announce the details of its new hospital insurance plan, these problems will be considered from the point of view of an employee welfare plan in Ontario.

Cancellation of Existing Hospital Benefits

According to the announcement made by the Ontario Hospital Services Commission, the Ontario plan is to become effective on January 1, 1959. Enrolment is compulsory for employers with 15 or more employees, and such employers will be required to register their employees under the Ontario plan by August 1958 and to pay the initial premium for that plan in December 1958.

Enrolment under the Ontario plan is optional for employees in groups of less than 15 and for individuals, and any employer with at least six employees may enrol as a group. However, it is important to note that the Ontario government is assuming exclusive occupancy of the basic hospital insurance field on and after January 1, 1959. In other words, no employer or individual may purchase hospital insurance up to the public ward level from any insurer other than the Ontario government. In effect this makes the Ontario plan compulsory for any employer unless he is prepared to do without hospital insurance entirely.

This provision is, of course, designed to enrol as large a proportion of the population as possible under the Ontario plan, and also to eliminate duplication of benefits to assist in control of costs. However, it removes entirely any freedom to choose between the government plan and private plans, and forces employers to revise existing plans, even where these have

been arranged through collective bargaining.

All employees in groups of six or more who are enrolled under the Ontario plan this year will become eligible for benefits on January 1, 1959, and this includes any employees or dependents who may be in hospital on that date. Normally, when a benefit is cancelled under a group plan underwritten by an insurance company, payment of benefits is completed for any claim incurred while the insurance was in force. For example, if an insured individual entered hospital before the termination of the hospital benefit, most insurance companies would continue benefits for the duration of the hospital confinement. Similarly there is usually a nine months extension for maternity claims under insurance company plans.

Since the Ontario plan takes over immediately on January 1, 1959, it should be specifically provided when cancelling the hospital benefit under insurance company group plans that no benefits will be paid for any hospital expenses incurred on or after January 1, 1959. This avoids duplication with the Ontario benefits, and is necessary in order to comply with the requirements of the Ontario plan. As this amendment may affect maternity claims where pregnancy commences as early as nine months prior to January 1, 1959, some insurance companies have considered that it is desirable to arrange for the amendment prior to March 31, 1958.

In order to make proper provision for the liability for claims already incurred, it is necessary for insurers to maintain at the end of each year what is known as a "reserve for open and unreported claims" and "a reserve for deferred maternity claims". The cancellation of benefits under group policies for hospital expenses incurred on or after January 1, 1959 will release the latter reserve and a part of the former reserve. Most insurance companies will probably give credit for the amounts released to group policyholders, either by a specific credit against premiums in December, 1958, or in the experience rating calculation on the next anniversary date of the policy.

Benefits under Ontario Plan

In addition to cancelling existing hospital benefits as required by the Ontario plan, employers will no doubt wish to consider what coverage should be purchased as a supplement to the Ontario plan, in order to produce in total benefits as good or better than those now in effect. It may be of interest, then, to compare the benefits provided by the Ontario plan with those of a typical group hospital insurance plan.

The Ontario plan as announced is to cover the full cost of the room and board charge for standard ward care and practically all special hospital services. The benefits are payable as long as the patient is confined to hospital without any maximum limit. Most private insurance plans have maximum limits ranging from 70 to 180 days, but unlimited benefits are possible under the government plan because it is subsidized to a substantial extent from federal and provincial taxation.

The Ontario plan does not, however, cover the fee for administration of an anaesthetic, nor the cost of diagnostic services outside of hospital. Out-patient hospital services for emergency admissions are covered when given within 24 hours of an accident.

The usual group hospital insurance plan provides a daily benefit of up to a specified amount such as $8, $9, $10 or even higher for the room and board charge for a maximum period ranging from 31 to 180 days. In addition, there is an allowance for special hospital services and for the anaesthetist's fee with a maximum limit which is usually a multiple (10, 15, or 20 times) of the daily hospital benefit. For example, if the daily hospital benefit were $10, the 15-times plan would provide up to $150 for the special hospital services and the anaesthetist's fee.

Blue Cross plans and some insurance company plans provide benefits on a service basis, that is, the cost of semi-private or ward accommodation is covered, whatever it may be, limited to a maximum number of days.

Gaps in Coverage

The first gap in coverage to be considered is the difference between the standard ward care provided and the level of hospital benefits now in effect. Many welfare plans are designed to provide approximately the cost of semi-private accommodation, and to maintain this level of benefits a supplementary daily hospital benefit would be required.

The actual cost differential between standard ward and semi-private accommodation is not yet definitely known, but it is understood that it may be about $3 for most hospitals. Most insurance companies will be prepared to include in group policies a supplementary daily hospital benefit of $3 to $5 per day to cover room and board expenses in excess of the Ontario plan on a reimbursement basis, for a maximum period up to 180 days.

Ontario Blue Cross has announced that it will have available a supplementary plan covering the cost differential for semi-private accommodation on an unlimited basis. It does, however, exclude sanatoria, hospitals for the chronically ill and mental hospitals. With a benefit of this kind a small increase in the extra cost for semi-private care would cause a proportionately large increase in claim costs, and inflationary trends would require prompt adjustment of premium rates.

Another gap in coverage is the anaesthetist's fee, now covered under the special hospital services part of insurance company group plans. A benefit for this item alone may be purchased from most insurance companies.

One other small area to be considered is the expense of X-rays required following an accident. These are usually covered under insurance company hospital benefits, whether taken at a hospital or a doctor's office. The Ontario plan will cover such X-rays only if taken as an out-patient at a hospital within 24 hours of an accident. A diagnostic X-ray and laboratory expense benefit may be purchased and this would cover not only X-rays under the circumstances mentioned, but also other X-rays and diagnostic procedures outside of hospital.

Cost Considerations

A typical group hospital insurance plan with a daily benefit of $8 for a maximum of 70 days and with 15 times the daily benefit ($120) for special hospital services would, in a group of at least 25 employees with less than 21% females and with normal experience, cost about $1.30 monthly for single employees and $4.85 for

married employees. Somewhat lower costs would prevail in large groups because of volume discounts, and in good experience groups because of experience rating refunds. The monthly premiums for the Ontario plan are \$2.10 for single employees and \$4.20 for married employees.

Obviously, the relative total costs of the two plans will depend on the proportion of married employees. As an example, let us assume a group of 100 employees, of whom 75 are married. The total monthly premium for the group hospital plan mentioned above would be \$396.25, while for the Ontario plan it would be \$367.50. The extra amount of \$28.75 monthly now being paid would be almost sufficient to purchase a benefit for the anaesthetist's fee which will not be covered under the Ontario plan. If it is desired to purchase the diagnostic, X-ray and laboratory expense benefit also, this would require an additional monthly premium of approximately \$45.

Because of the substantial subsidies to the Ontario plan from federal and provincial taxation, subsidies which are estimated to pay about two-thirds of the cost, it might be expected that the premiums charged for the Ontario plan would be materially lower than under existing hospital plans. Such, however, is not the case for most groups. Probably the chief reason for this is that the Ontario plan is available to all, regardless of state of health or age, and it may be anticipated that among those for whom the plan is optional the less healthy individuals will apply more promptly and in greater numbers. The resulting higher claims cost must be provided for in setting the uniform premiums to be charged to all. A second reason is that benefits under the Ontario plan are unlimited as to duration, but this is a relatively small factor in the total cost.

It is clear, then, that in the average group if the present hospital benefit is about \$8 on the 70 day - 15 times plan, the total cost for the Ontario plan plus an anaesthetist's fee benefit will be about the same as the present outlay. However, if the present plan has greater benefits or provides semi-private accommodation, some margin would be available to purchase benefits supplementary to the Ontario plan at about the same total outlay as at present. For the average group a supplementary daily hospital benefit of \$3 per day for 120 days, which should approximately cover the extra cost of semi-private accommodation, would cost about 35c monthly for single employees and \$1.25 monthly for married employees from an insurance company. The Blue Cross supplementary semi-private benefit will cost 55c monthly for single employees and \$1.10 monthly for married employees.

Comprehensive Benefit

The very newest development in group health insurance is the comprehensive health insurance plan, sometimes referred to as comprehensive major medical insurance. This modern plan affords an ideal means of supplementing basic government hospital coverage.

The comprehensive plan has the following characteristic features:

1. It does not limit benefits to specific sources of charges, but rather uses the blanket approach and embraces all reasonable and necessary expenses for medical care and treatment.
2. It provides reimbursement up to

substantial limits, and protects against catastrophic medical expenses.

3. It has an initial deductible applicable to first-dollar charges and all expenses beyond the deductible are subject to coinsurance.

A typical comprehensive plan might have a deductible of $25, applicable to expenses incurred by each individual in any one calendar year. All expenses in excess of the deductible would be subject to coinsurance, that is, such expenses would be reimbursed to the extent of 80%. The maximum benefit for each person might be $5,000 or $10,000. The plan would apply to hospital expenses, physicians' and surgeons' fees, prescribed drugs and medicines, special nurses, anaesthetics, X-ray and diagnostic services, and any other reasonable and necessary expenses for health.

To adapt the comprehensive plan to supplement a government hospital plan is simple, as it is merely necessary to exclude the expenses covered by the government plan and to reduce the premium rates accordingly. The result is a plan providing complete health insurance in one simple package.

For an average group the cost of a comprehensive plan to supplement the Ontario plan with a deductible of $25, coinsurance of 20%, and a maximum benefit of $5,000 would be about $1.90 monthly for single employees and $7.00 monthly for married employees. This cost would vary with the size of the group, age distribution of employees and other factors, and could, of course, be materially reduced by increasing the deductible to $50 or $100 and the coinsurance to 25%. This cost in total would approximate the cost of a supplementary hospital benefit of $3, an anaesthetist's fee benefit, a diagnostic benefit, and a good surgical and medical plan.

Because the public has become accustomed to first-dollar coverage, it might be expected that there would be some reluctance to substitute the comprehensive plan for the conventional basic benefits. While this has been experienced in some quarters, there is a growing public acceptance of this plan, and its merit of covering all types of expense and providing very large benefits for serious and needy cases is coming to be recognized. The necessity of revising present welfare plans because of the introduction of government hospital insurance presents a real opportunity to modernize and consolidate these plans through the comprehensive approach.

Plans in Other Provinces

In the above discussion we have referred particularly to the government hospital plan to be adopted by the Province of Ontario. At the date of writing, the following information is available with regard to plans in other provinces:

British Clumbia – A plan is now in effect providing benefits similar to Ontario, less a daily deterrent fee of $1. No premiums are charged to residents, and the plan is financed through a sales tax.

Alberta – A plan was made effective April 1, 1958, providing benefits similar to Ontario, less a daily deterrent fee varying from $1.50 to $2, according to size of hospital. The plan is to be financed from provincial revenues with no direct premium charge.

Saskatchewan – A plan is now in effect providing the same benefits

as the Ontario plan. Residents are charged an annual premium of $15 for adults and $5 for children, with a family maximum of $40.

Manitoba – It is understood that a plan similar to that of Ontario was introduced on July 1, 1958.

Quebec – No announcement has been made regarding the introduction of a government hospital plan.

Maritime Provinces and Newfoundland – It is expected that these provinces will introduce a plan in the near future, but details are not yet available.

Employers with employees in a number of different provinces will be faced with the problem of adapting existing welfare plans to the varying terms of different provincial plans in regard to benefits and premium charges. It will no doubt de desired to achieve a reasonable uniformity of total benefits and an equitable sharing of costs in the different provinces.

The comprehensive benefit mentioned above seems to provide a very satisfactory way of arranging benefits which are approximately uniform. Any differences in benefits under provincial plans will fall into the area covered by the comprehensive benefit and the premium rates for this benefit would vary slightly between provinces with differing plans. An alternative would be to adjust the supplementary hospital benefit between provinces in accordance with the different provincial plans.

In determining the basis of sharing costs between employers and employees consideration will not doubt be given to the sources of revenues for financing the various provincial plans. In Ontario, for example, it is indicated that about 2/3 of the cost will be financed from provincial and federal revenues, to which employers are contributing substantially through the corporation tax. This aspect of the problem will require careful study and cost analysis if costs are to be shared equitably by employees in different provinces.

Canadians too Conservative in their Investments?

There is no evidence to indicate Canadians are either more or less conservative than Americans in their investment policies. But the population of the United States is ten times as large as that of Canada, and per capita income in that country is approximately 20% higher. Thus in the United States there is a much greater supply of capital than in Canada. While U.S. capital forms a relatively large share of the total investment in Canadian industry, the sum involved is small in comparison with total industrial capital in the United States. To illustrate the importance of this factor of size, Canadian direct investment in the United States, at the end of 1955, while only a very small part of total business investment in that country, was on a per capita basis twice as much as U.S. direct investment in Canada.

– W. M. V. Ash, president, Shell Oil Co. of Canada Ltd., to the 5th Western Canada Conference on Financial Management and Petroleum Accounting, Banff, May 1958.

THE SMALL STORE:

Accounting Procedures

C. A. KING

THE SMALL STORE, for the purposes of this article, may be defined as any retail establishment with a staff of between five and twenty employees, and an annual turnover of between $100,000 and $500,000, depending on the type of merchandise handled. Within the scope of this definition, the manner in which business transactions are recorded, the frequency with which informative financial statements are prepared, and the resulting degree of efficiency shown by management will vary widely. In this highly competitive age, even a slight variation in the degree of operating efficiency maintained by the small store owner can mean the difference between financial stability and bankruptcy.

Not so many years ago, when communities were somewhat less interdependent than they are today, the small retail business with an established clientele enjoyed a relatively secure competitive position. As a result, management was not so concerned with operating costs. Working capital was usually maintained at a fairly uniform level, and the need for detailed analytical information from the accounting records was not particularly acute. At year's end, unless the profit and loss statement showed a sharp decline in sales and net profit, the figures contained therein were seldom subjected to close scrutiny by the owner. Remedial action probably would not be taken until the store's working capital had been reduced to the point where it meant curtailing the profit distributions or proprietor's withdrawals. With ever increasing improvement in transportation and communication facilities, as well as the complexity of modern merchandising, the successful small store owner of today must be an able administrator. This he cannot be unless he has at his fingertips up-to-date information relating to the store's operations so that he can make prompt, intelligent decisions concerning such matters as cash requirements, seasonal trends, margins, overhead, purchasing and sales policies. This is one reason for the growing importance of maintaining adequate accounting records in the small store.

Governmental Influence on Accounting Procedures

With the advent of personal and corporation income taxes in this country, and the ensuing insistence on the part of taxation authorities that individuals and corporations meet the

minimum legal requirements relating to the keeping of records necessary to determine income accurately, further impetus has been given to the improvement of accounting procedures. Other federal and provincial government agencies, too, have helped to enlarge the small store owner's bookkeeping staff. These include the Dominion Bureau of Statistics, the Unemployment Insurance Commission, provincial Workmen's Compensation Boards and sales tax authorities. Having to maintain records in greater detail for others, surely the store owner can turn necessity to his own advantage.

To illustrate the impact of government legislation on the accounting procedures maintained in a small store, let us examine the effect of a provincial sales tax on the recording of sales. This is a particularly timely example, as many Canadian provinces have recently entered the sales tax field or are presently considering such a levy.

The small store owner at first may apply harsh epithets to such a tax imposition, for it devolves upon him to collect this tax on behalf of the government, keep accurate and detailed records of such collections, and remit to the government at regular intervals.

Once the rate of sales tax has been established and the relevant legislation enacted, the first task confronting the retailer is to familiarize himself with a complete list of taxable and non-taxable items of merchandise. Usually, certain "necessities" and purchases below a stated amount are exempt from sales tax. Therefore, sales records must be maintained on a "taxable" and "non-taxable" basis to facilitate checking by sales tax auditors. The next question relates to charge sales. The store owner must know if he is liable for remittance of tax on charge sales as soon as the sale is completed or later, when the account is paid. If later, then it will be necessary to devise some method of ensuring that the sales tax liability is promptly recorded in connection with all receipts on account. In acknowledgment of the collector's role played by the retailer, the sales tax authority usually allows him a small commission on collections. Thus, this percentage of collections must be periodically transferred to a revenue account. Then, too, arises the question of sales tax on goods taken from stock for the owner's personal use. All in all, the chief result of a provincial sales tax imposition is to compel the small store owner to maintain detailed sales records; but he may turn the requirement to his advantage by extending the sales analysis further to produce figures highly informative to himself. Such analysis might distinguish between classes of goods, cash and credit sales, advertised and non-advertised lines, or similar revealing breakdowns.

Types of Accounting Systems

Once convinced of the necessity of maintaining records that will furnish him with useful data when it is required, the small store owner is confronted with two or three alternatives as to the best manner in which this goal may be achieved. At the lower end of the small store classification, e.g. the store with a staff of five to ten employees, the owner or manager may supervise the bookkeeping procedures and actually write up and total the books of original entry. These would probably consist of a cash or day book for daily receipts and disbursements, a

purchase book for invoices from trade creditors, and a sales book for charge sales. One of his clerks could be responsible for posting charges and payments from these books to the subsidiary ledgers of receivables and payables. The nature and design of these records should be prescribed at the outset by a qualified accountant so that the most useful information will be produced with the minimum of effort.

Somewhat higher in the scale, it will be found desirable to employ a competent full-time bookkeeper, with a clerical staff of two or three, if necessary, to perform the routine accounting procedures such as the checking of purchase and sales invoices and the posting of subsidiary ledgers mentioned earlier. The bookkeeper's duties will include posting the general ledger, reconciling all bank accounts and preparing a monthly trial balance. Among those retail stores whose annual sales approach $500,000, it might be advantageous because of the saving of time and the elimination of posting errors to consider mechanizing the accounting system, at least in part.

Frequently, the small store owner decides against enlarging his staff to meet accounting requirements. In some instances, the choice may not rest with him as there might very well be a dearth of qualified bookkeepers in his community. In such circumstances, many small stores have their books written up weekly or monthly by professional bookkeepers or practising chartered accountants. The volume of professional services to be performed and the responsibility to be assumed therefor will depend on individual circumstances, but mutual understanding on this important matter should be assured by an exchange of correspondence between the parties.

Some professional accountants may conduct a large part of their bookkeeping services by mail, providing the client with a month's supply of simple journal forms for cash receipts and disbursements, charge sales, purchases, etc. A few minutes' effort on the part of the client every two or three days will suffice to complete these. At the end of the month they are mailed to the accountant, who adds and balances them, posts the general ledger, notes any items requiring immediate clarification or discussion with the client, and repeats this procedure monthly until the fiscal year end arrives. Under this system, the store's staff would be responsible for maintaining the original records relating to business transactions, such as sales slips, cash register tapes, deposit slips, and cheques issued, handling all receipts and payments in the usual way, and posting the subsidiary "personal" accounts, receivables and payables. Where the owner considers it economically sound to do so, he may include in the professional accountant's functions such duties as billing customers monthly, the preparation of payrolls and the cheques relating thereto, the reconciliation of accounts payable with creditors' statements after checking of individual invoices with merchandise receipts has been completed, and the answering of letters directed to the attention of the accounting department.

In order to determine the relative cost of certain accounting procedures as performed by his own staff and as done by the staff of a professional accountant, the small store

owner will usually ask the latter to quote him or to estimate a weekly or monthly fee. It may be necessary for the accountant to serve on a "trial fee" basis for a few weeks or months until he has become thoroughly conversant with the client's routine and the multifarious details that can be expected to recur at regular or irregular intervals. Once he knows with a fair degree of accuracy just what the store owner expects of him and his staff, and the average length of time required, he will be in a position to quote the requested fee.

Whatever approach to the bookkeeping problem is adopted, it is important that current figures be produced reliably and promptly, that the data be adequate for government and credit purposes, and that the statements facilitate intelligent planning for the enterprise.

Monthly Financial Statements

Today's small store owner should be vitally concerned with the economic significance of the figures contained in his operating accounts. Thus, the preparation of those figures, although an important procedure in itself, is but a prelude to the preparation and interpretation of financial statements to assist management in its efforts to maintain or improve the store's financial position. We have discussed the role of the professional accountant in fostering efficient accounting methods. In addition, he has a moral obligation to make available to his clients the benefits of his special knowledge stemming from his broad professional experience. Because he can obtain and interpret statistics and percentages of gross and net earnings of other retail stores in the same line of business across the country, he can compare his clients' operating results with the average for the nation, or perhaps in the immediate area. Any appreciable difference can be analyzed in detail, until the cause of excessive costs or lower sales is understood. Another advantage accruing to the small retailer, from the employment of a professional accountant in preference to using his own accounting staff for the purpose of preparing comparative financial statements, is the unbiased viewpoint the former brings to bear.

The most effective way in which comparative dollar amounts can be presented for quick study involves the use of percentages or graphs. With the key figures reduced to percentages, the significance of gross profit ratios, of the relationship of cost of sales to sales, and of operating costs and net profit to sales becomes much clearer. Similarly, a line or bar graph is worth scores of words in drawing to the store owner's attention visually the relationship between figures. Graphs are probably the most lucid means of revealing the long-term trends inherent in his business and the results to be expected if present policies are pursued.

On a monthly or four-week basis, comparative financial statements can be of immense value in making management immediately aware of any departure from the normal. In the preparation of such statements, there is one asset, affecting both the balance sheet and the trading statement, the valuation of which is the most susceptible to error or difference of opinion. This is the inventory of merchandise on hand. This whole controversial question of the various methods of merchandise control and valuation will be discussed in considerable detail in a subsequent

article. Suffice it to say, for present purposes, that the small store owner's inventory valuation will in only a few instances be taken from reliable perpetual inventory records. In the absence of such records, a conservative estimate of merchandise on hand must be made, supplemented by occasional physical counts. There is the very real danger, though, that estimated inventories will not be checked sufficiently against actual merchandise and that the amount of such inventories will be determined primarily by gross profit requirements rather than by reality. If the inventory is not closely estimated, the chief purpose of preparing monthly operating statements can be defeated.

Where more than one class of merchandise is handled, or where various qualities of merchandise are sold at different margins, the records should be classified so that sales, purchases and inventories are ascertainable for each type of merchandise or each department. Thus, if any item is not paying its way, it can be discontinued or steps can be taken to make its sale profitable.

Annual Financial Statements

The accountant who has been supervising a store's accounting procedures on a weekly or monthly basis and preparing monthly financial statements on his client's behalf is at a distinct advantage at the fiscal year end. He can prepare the annual statements with a minimum of delay, for the work he has performed during the year, being of a combined accounting and auditing nature, will probably have reduced the amount of checking he would have to do in order to express an opinion upon the correctness of the year end statements he has prepared. In addition to the balance sheet and profit and loss statement prepared each month, the annual statements will be made more valuable if they include several supporting schedules and analyses interpreting various phases of the year's operations. The professional accountant can be particularly helpful to his client if in his report or a separate letter he mentions special or significant items that have come to his attention during the current period, especially if it appears that they will affect subsequent periods.

Recommendations may also be made at some length as to ways in which operating results can be improved in the future. During the year, one ratio that may not receive special attention is that relating to working capital. This is the comparison of current assets to current liabilities, and often a satisfactory ratio is about two to one. An analysis of working capital changes during a period is usually made clearer when presented as a statement of available funds and the use to which they have been put during that period. Businessmen considering future plans will be governed to a large extent by these figures, and forecasts on a similar basis for the months ahead, for the firm's present and potential liquid position, will determine the rate at which the store can safely expand, spend money on capital improvements, or make capital or profit distributions to the owner or owners.

The store owner will usually require an accountant's certificate or report with his annual financial statements for several reasons, or rather for several variations of one reason. Those parties having access to his statements all want assurance that they have been prepared by a

competent, independent accountant, whether the parties concerned are shareholders, credit grantors, the Taxation Division of the Department of National Revenue or some other governmental body.

The individual store owner should apply those bookkeeping methods and policies most likely to improve his economic prospects, and this usually means discarding his traditional antipathy to paper work. Once he has learned to appreciate the end figures produced by a set of books competently designed and maintained, he will never again wish to be without the vital help they give him.

Productivity

There has been a great deal of talk about Russia's new weapons—nuclear bombs, intercontinental missiles, submarines and the like. There is, however, another and more basic weapon on which the Kremlin relies. Its name is productivity.

The Soviet Government has not released figures on productivity per worker but there can be no doubt it is increasing. One estimate gives an increase of 6% in the first half of 1957, as contrasted to the corresponding period of 1956. In the United States, the increase in productivity per man in industry in 1957 was only 1.2%, while in Canada it may actually have fallen. In both these countries, as a result, the numerous wage increases demanded and granted have been immediately reflected in higher prices.

If this trend continues, the Kremlin's dream of surpassing the United States in industrial production may quite conceivably be realized within the lifetime of the present generation. Increasing quantities of relatively low-priced Russian goods will compete with high-priced North American goods in the markets of the world; while the Soviet Government will have an ample backlog for aid programs designed to influence undeveloped nations in Africa and Asia.

It was in Britain and the U.S. especially that the idea first took root that the way to individual and national prosperity was through hard work, saving, increased skill and the steady improvement of tools and machinery. Yet somehow this conception, which seemed so clear to our ancestors, has been dropped by the wayside.

In the English-speaking world, at least, the notion prevails that the road to riches lies through installment buying, shorter hours of work, wage demands that bear no relation whatever to increased productivity, and frequent strikes. As long as we are weighed down by these illusions, we can hardly hope to win the race to which Moscow is challenging us.

—**Extract from** ***Globe*** **&** ***Mail.*** (Editorial), May 2, 1958

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Trends in Canadian Financial Reporting

Gertrude Mulcahy, C.A.

The subject of annual financial reporting has occupied the attention of accountants, managements, investment analysts, financial commentators and financial advisers for some time. Their efforts to develop and promote effectiveness have produced outstanding results. In recent years, the annual report has undergone a remarkable improvement. The basic principle has become firmly established that shareholders, both actual and potential, are entitled to know as much as possible about their companies and to have the facts presented to them in a manner in which they can understand.

Canadian annual reports have kept pace with this striking trend towards effectiveness. Each year, more and more companies are striving conscientiously to give their shareholders and customers a full picture of what has been going on in the past, where the company stands now, and what are the prospects for the future. To encourage good reporting in Canada, *The Financial Post* has, for several years, offered awards for the best reports. In announcing the results of the 1957 contest, it was reported that "Canadian corporations did a better job than ever before" and one of the judges commented that "A gratifying large number of companies had found a way to a happy compromise between the twin problems of annual reporting – presenting the various financial statements, ratios and statistics needed by the professional who would make an intelligent analysis of the company, and telling the story in a reasonably simple way which will not repel unsophisticated shareholders."[1]

In competition with annual reports of companies in other countries, the Canadian submissions have made an excellent showing. For a number of years *The Financial World,* an American investment and business weekly magazine, has conducted a survey of annual reports of companies from the United States and Canada and awards are given for distinguished achievement in the various industrial classifications. Some 5000 reports were entered in the 1957 contest. A fairly lengthy list of Canadian companies was in the awards list and a number won recognition in their respective fields.

Of the 109 bronze oscars awarded for the annual reports judged best in each industrial classification, 3 were won by Canadian companies: Hiram Walker-Gooderham & Worts, Ltd. in the distilled spirits section, St. Lawrence Corporation Ltd. in the pulp and paper section, and Southam Co. Ltd. in the publishing section. The group of 218 companies ranking second and third best in the respective sections included Trans-Canada Air Lines Ltd., Aluminum Ltd., Ventures

[1] *The Financial Post,* November 16, 1957.

Ltd., Cockshutt Farm Equipment Ltd., Canada Packers Ltd., Scudder Fund of Canada, Moore Corporation, Home Oil Co. Ltd., and MacMillan Bloedel Ltd. One Canadian company has established an outstanding record in this contest: Chateau-Gai Wines Ltd. was an award winner in 1957, making the tenth year in a row that it has submitted a report which has attracted the favourable attention of the contest judges.

The focal point of all annual reports is the financial statements themselves, and it is by the development of effective techniques of presentation and disclosure within these statements that accountants and accounting societies have made a definite contribution to the remarkable improvement in annual reporting. "Financial Reporting in Canada," 2nd ed., 1957 provides a fairly complete summary of the recent trends and developments in financial reporting and accounting practices in Canada. The statistical tabulations indicate that, in some aspects, a high level of effectiveness has been achieved, but that in others there is still room for improvement and greater uniformity and understanding.

Outstanding Improvements

The following are some of the areas in which high standards of practice have been established and maintained.

Classification of Items in Balance Sheet

The Committee on Accounting and Auditing Research of the Canadian Institute of Chartered Accountants recommended in Bulletin No. 14 that "Accounts should be segregated in a balance sheet according to the accepted distinctions such as current assets, fixed assets, current liabilities, long-term debt, shareholders' equity." Because of the differences in circumstances peculiar to the individual companies and because of fluctuations in accounting practices which have not yet been finally accepted or rejected, it is reasonable to expect that there would be a certain amount of variation in the classification of items. However, a very high degree of effectiveness and uniformity in practice has been achieved in providing recognition of the basic distinctions recommended in Bulletin No. 14. In each of the four years analyzed (1953 to 1956 inclusive) this was accomplished, in over 98% of the balance sheets, by the grouping of items of a similar nature under descriptive captions. The extension of sub-totals and totals of the various groups was almost uniformly adopted, although a few cases were noted in which this procedure was not followed and the segregation was effected by the use of designating captions only.

Not all of the balance sheets referred to above provided ideal and complete classification of all balance sheet items. The form of presentation of the shareholders' equity is the outstanding flaw in the general acceptance of adequate classification procedures. However, the standards in this area are fairly good and have shown improvement over the last few years. In 76% of the balance sheets analyzed for 1953, an effort was made, by way of designating captions, groupings and extensions of totals, to identify the shareholders' interest in the company's assets. By 1956, this percentage had increased to 81%. One of the faults in annual reports, noted specifically in the 1956 *Financial Post* annual reports award, was the failure to label, as such, the balance sheet

items which make up the shareholders' equity. In 1957, one of the judges noted that more companies were eliminating this deficiency and providing proper classification of the items concerned. It is to be hoped that the trend towards better presentation of this portion of the balance sheet will continue and that the practice of grouping the component items under a descriptive caption with a single total extended will become generally accepted. It has already received strong support: 73% in 1956 as opposed to 63% in 1953.

Consolidated Statements

Although Canadian public companies are not required, either by statute or by Securities Commission rulings, to prepare their annual financial statements on a consolidated basis, this practice has become well established as one of the basic principles of effective financial reporting. "In 1953, 83% of the parent companies prepared their annual financial statements on a consolidated basis. By 1956, this percentage had increased to 88%, with 71% on a fully consolidated basis and 17% on a partially consolidated basis".[2]

It is recognized that consolidated statements do not always give the shareholders of the parent company the fairest picture of their investment. But it has been recommended that where subsidiaries have not been consolidated, the reason for the exclusion should be clearly stated. Unfortunately, the practices in this respect have varied, with less than 50% of the 1956 reports concerned providing this information.

Inappropriate Uses of the Term "Reserve"

One of the most outstanding trends brought out by the statistical tabulations of "Financial Reporting in Canada" is the marked decline in the inappropriate usage of the term "reserve". In 1956, only 15% of the 300 balance sheets analyzed made use of the term in describing one or more of the following items: allowance for doubtful accounts, accumulated allowance for depreciation and estimated liabilities for income taxes. This decline from 41% in 1953 indicates without a doubt that accountants and management recognize the wisdom of the recommendations of Bulletin No. 9, that the term "reserve" be limited to segregation of earned surplus and "not be used to designate amounts provided in respect of actual liabilities, deferred income or diminutions in the value of assets". (Bulletin No. 9, January, 1953) When compared with such percentages as 67% re doubtful accounts and 69% re depreciation in the statements analyzed for 1952, immediately prior to the release of Bulletin No. 9, the decline is even more outstanding and represents a real achievement.

Details of Long-Term Indebtedness

A predominant practice of disclosing the interest rate and maturity date of at least part, if not all, of the long-term indebtedness has been exhibited in the balance sheets in recent years. Over 96% of the balance sheets showing long-term indebtedness, in each of the four years 1953 to 1956 inclusive, have provided this information each year. In addition, of the balance sheets indicating maturity of part of its indebtedness within one year, at least 96% each year disclosed the amount of such maturities. In the original pronouncement on minimum standards of disclosure, Bulletin No. 1, October 1946, the Committee on Ac-

[2] "Financial Reporting in Canada", 1957.

counting and Auditing Research stated that "Unless shown separately under current liabilities, the amount of bonds payable or the amount of the sinking fund payment due within the succeeding year should be disclosed." In the revision of this bulletin, in August 1957, the committee was somewhat more specific and recommended that "The amount payable within a year out of current funds in respect of long-term debt should be included in current liabilities." This latter suggestion had, in fact, become an established procedure prior to this pronouncement with at least 80% of the balance sheets concerned following this method of disclosure in each of the years 1953 to 1956 inclusive.

DETAILS OF SHARE CAPITAL

The statistical tabulations relating to capital stock show almost unanimous adoption of the practice of disclosing the details of share capital authorized, nominal value of shares, and number of shares issued. In addition, in the vast majority of cases, the rate of dividends on preferred stock was disclosed (90% in 1956, 91% in 1953). Of the balance sheets indicating a change in share capital during the current year, 93% in 1956, disclosed the actual details of such changes. Compared with 73% in 1953, this increase shows a continued effort to provide adequate information. A marked preference has been exhibited for disclosure of such details in the balance sheet itself or in notes appended thereto.

Unfortunately the need for segregating the amount of share capital outstanding for each class of share where there are more than one class of shares has not received as widespread recognition. Although the predominant practice is to provide this segregation, the proportion of balance sheets which grouped the amount for two or more classes in one figure has increased slightly in the last few years (24% in 1956 as opposed to 20% in 1953). This change is in the opposite direction to those reflected in other aspects of capital stock presentation. Disclosure of redemption price where shares are redeemable has not become generally accepted procedure. This may be influenced by the opinion that disclosure of price is not necessary where the shares are redeemable at par.

DIVIDENDS AND EXPENSES

The Company's Act (Canada) requires that the statement of surplus should show "dividends paid or declared on each class of shares, stating the account against which the same are charged". Disclosure of this information is accepted practice, with only 9 out of 300 companies in 1956 combining the dividends on more than one class of shares into one figure.

Disclosure of the amounts charged for depreciation, interest on indebtedness and taxes on income, either as separate items in the statement of profit and loss or in a footnote to such statement, is well established as standard procedure. On the other hand, practices relating to dividends from subsidiaries' minority interest in profit and loss of consolidated subsidiaries and unusual and non-recurring items varied, although definite preferences were indicated.

Gradual Improvement

In some parts of the financial statements only a slow improvement has been shown, and there is still need for wider adoption of those practices which have been established as desirable and adequate.

SUPPLEMENTARY STATEMENTS AND SCHEDULES

The proportion of companies providing supplementary summaries, statements and schedules is increasing but not very quickly. This practice, unfortunately, has not as yet reached the stage at which it would be classified as generally accepted. The statistical tabulations show the variety of statements used to disclose the historical background of the current financial statements.

COMPARATIVE STATEMENTS

Financial statements on a comparative basis, i.e. showing the corresponding figures for at least the preceding year in addition to those for the year under review, are presented by more companies each year. While this practice cannot as yet be classified as generally acceptable, (56% in 1956), the proportion presenting some or all of the financial statements on a comparative basis has increased 16% in the last four years.

BASIS OF VALUATION OF ASSETS

In Bulletin No. 14, the committee stated that "The basis of valuation of assets should be explicitly disclosed where the basis is not self-evident." A review of the statistical tabulation relating to the various assets discloses that this practice is generally followed, but that there are some specific items for which a significant proportion of the reports do not provide this information: marketable securities, investment in subsidiaries, other investments, goodwill and intangible assets. In each of these items there has been a gradual decrease in the number of reports which fail to disclose the bases of valuation, but percentages of 27, 44, 33, 22 and 18 respectively, on the reports for 1956, indicate the need for greater attention to this matter.

CLASSIFICATION OF RESERVES

Unfortunately, the recommendation of the committee that reserves be shown as part of the shareholders' equity has not as yet received the same high degree of recognition and acceptance as was accorded the suggestions relating to the inappropriate use of the word "reserve". By 1956, only 34% of the balance sheets showing reserves on the liability side included them as part of the shareholders' equity. Although this percentage had increased from 24% in 1953, it does not indicate a rapid trend toward the presentation which the committee considered to be most desirable.

In contrast, transfers to and from reserve have generally been treated as adjustments of earned surplus, as recommended in Bulletin No. 9.

STANDARD FORM OF AUDITOR'S REPORT

Although there has been a definite trend towards the use of the standard forms of auditor's report recommended by the committee in 1951 and 1954, a surprising number of reports still do not adhere to the suggested wordings (37% of Dominion companies and 46% of Ontario companies in 1956). Many of the reports classified as not conforming with the standard form did not differ significantly but reflected personal preferences in terminology rather than differences in content of the report. Examples of such variations have been set out in the commentary on table 53 in the second edition of "Financial Reporting in Canada".

Improvements Needed

The following are some of the outstanding deficiencies in published financial reports in this country.

SOURCES OF SURPLUS

The recommendations of the Com-

mittee on Accounting and Auditing Research released in August 1955, as to the segregation of surplus items between "earned" and "contributed" surplus, have not as yet become generally accepted although there has been a slight increase in the proportion of balance sheets providing this classification. In 1956, only 25% of the balance sheets showing more than one surplus item followed the recommended practice.

Sales

As yet, very few Canadian statements disclose annual sales, even though the inclusion of sales or net sales in the details of the statement of profit and loss has become standard practice in published reports in the United States. The judges of the 1957 *Financial Post* annual report awards noted that "more companies are disclosing their gross sales or revenue figure in their earnings statements, but their number is increasing too slowly." Table 43 of "Financial Reporting In Canada", 2nd ed., 1957, shows that in 1956 only 85 out of 300 reports disclosed the sales figure.

Basis of Income Tax Deduction

In September, 1954, the Committee on Accounting and Auditing Research presented what they considered to be an acceptable solution to the problem of income measurement created by the repeal of Income Tax Regulation 1100(4). The committee recommended that the current tax savings resulting from claiming excessive capital cost allowances should be deferred to be applied to those future years when depreciation corresponding to the excess is charged in the accounts. In 1956, 37 of the 300 companies analyzed adopted this suggested treatment with 24 others following the alternative treatment suggested in Bulletin No. 10, i.e. current tax saving treated as an increase in reported net profits, with the effect of the reduction in taxes payable on net profit for the year set out in explanatory footnotes on the financial statements. In a proportion of the remaining cases it was difficult and sometimes impossible to tell, from the information provided, whether or not the computation of reported net income had been affected by current tax savings, although in some instances it was definitely stated that there was no problem since depreciation and capital cost allowances were the same.

Terminology re Net Profit

A wide variety of terms are used to identify the closing balance in the statement of profit and loss, as well as the balance transferred from yearly operations in the statement of earned surplus. While definite preferences have been exhibited, the variations appearing in the published statements might well cause confusion to those readers unfamiliar with accounting terminology and expressions. The statistical tabulations in respect of each of these balances clearly show a lack of uniformity in this connection.

Edited by **CAMPBELL W. LEACH, C.A.**

Tax Review

The Budget

On Tuesday, June 17, Finance Minister Donald M. Fleming presented his first budget to the House of Commons. The budget speech was very lengthy and provides an insight into the complexities of a modern economy. The conflicting forces which operate within and without the country and the difficulty of weighing their significance leave the layman with the feeling that economics is one field in which there are few well defined guideposts. Among other things, Mr. Fleming observed that during 1957 the average annual earnings per paid worker rose by 4% although the increase in the gross national product was negligible and corporate profits declined by 11%. Our economic dependency on the United States was also referred to, and there is an unavoidable impression that our internal fiscal and monetary policies can do little more than smooth out the peaks and troughs of our economic progress over which we have less control than we would like to have.

Mr. Fleming forecasted budgetary revenues at $4,660 million and budgetary expenditures at $5,300 million for a deficit of $640 million, without any changes in the tax laws. Confronted with such a large deficit and a less than buoyant economy, the Finance Minister was not prepared to propose tax reductions in excess of $8 million on the grounds that the problems of a recession could not be resolved by tax reductions alone. In his opinion, the best prescription for our present economic slump requires three ingredients: the tax relief given last December, the program of public investment which has been underway for several months, and income maintenance policies involving increases in old age pensions, veterans' benefits, unemployment insurance, etc. which were also adopted late last year. In this connection, Mr. Fleming made the following observations:

"The advocates of tax reductions argue that by leaving more money in the hands of individuals, consumer spending will be stimulated and more savings will be available for productive capital investment. But I believe experience has shown that while this may happen to some extent, unless other stimulating measures are taken, much of the tax saving to many taxpayers tends to lie idle. It is neither wholly spent nor put into productive investment.

"A program of public investment has the obvious advantage of providing employment for idle or underemployed manpower and equipment. But it cannot be a complete answer. In a country as large and as economically diverse as Canada it takes time for some programs to exert their maximum benefit upon the under-employed resources of the secondary industries and of many districts.

"The third approach to the problem —the extension of income maintenance policies — has the essential value of

relieving hardship and somewhat equalizing the burdens of recession, but apart from maintaining a reasonable level of consumer spending, such measures make a limited positive contribution to the resumption of healthy economic expansion."

Although many taxpayers may be willing to concede that these statements seem entirely reasonable, they nevertheless create a feeling of frustration, if not despair. For if in prosperous times tax reductions must be postponed because of their inflationary impact and if during recessions tax reductions should be postponed in favour of public works and security transfer payments, then many taxpayers may be inclined to draw the not illogical conclusion that tax reductions require a very uncommon balance of conflicting economic forces. How this can be brought about is anybody's guess but it would appear that a more widespread appreciation of Mr. Fleming's remark that ". . . . increases in incomes can be justified by increased productivity and by increased productivity alone" would be a step in the right direction. Nevertheless, no matter how many more goods and services are produced, if the nation's demand for social security also increases at an equal or faster pace and the costs of national defence continue to climb, the tax-paying public may find itself on a fiscal treadmill for some years to come. It might have been expected or even hoped by some that a Conservative Minister of Finance, confronted with a considerable deficit, would have expressed doubt as to how long "welfare state" expenditures could be allowed to increase, instead of endorsing them.

Superficially, our post-war experience would seem to suggest that a very high level of taxation may be a permanent phenomenon in a prosperous and socially conscious country. However, should the national output increase at a more rapid rate than government expenditures, it would seem reasonable to expect that tax rates could be reduced and still provide the government with adequate revenue. It is to be hoped that this likelihood is not so far in the future as to preclude the possibility that many of our present taxpayers will be around to celebrate the occasion!

* * *

Closely Held Corporations

The necessity for tax planning in the day-to-day management of a company hardly requires any emphasis. As soon as a corporation's income reaches the level at which it is retaining only 53% of its earnings, it is to be expected that there will be an acute awareness of the need to minimize taxable income whenever possible. This should not be the only objective of tax planning, however, particularly in the case of a closely held corporation. Although a corporation is always a separate legal entity, when it is owned by one or a small group of persons it is important for the shareholders to realize that their investment is affected by considerations which usually do not influence an investment in the shares of a widely held public company.

Often an individual will incorporate a private company and, by initiative and hard work, build up a successful business. In its early years, as the business is expanding, he may be satisfied to forego dividends and year after year plough back earnings until the company is financially secure and has a large balance of retained earnings, or undistributed income, as it is

officially referred to in the Income Tax Act. Once the business is well established and the principal shareholder is drawing an adequate salary, he frequently is content to have the company continue the accumulation of retained earnings due to the fact that, if they were paid out to him as dividends, a substantial portion of such dividends would be payable to the Receiver General of Canada. Unfortunately, chances are the Receiver General will receive his share sooner or later and postponement of the evil day may only increase that share and create problems all too frequently ignored.

With advancing years, the owner of a successful private company may find that it would be in his best interest to dispose of his company. If its fixed assets are undervalued and it has been earning an above average return on the capital invested in it, he may very well expect to be able to sell his shares for a price considerably in excess of their "book value" and realize a handsome capital gain. However, as far as a prospective purchaser is concerned, it is seldom that he will pay as much for shares as he would for net assets. For one thing, if the price of the shares reflects an increase in the value of the assets, it will not benefit the purchaser since this increase in value will not be depreciable.

Difficult though it may be to resolve this conflict of interests, if the value of the shares does not contain a substantial amount of undistributed income, a meeting of the minds between vendor and purchaser as to the price of the shares usually can be arranged without too much haggling. However, if there is a large undistributed income it aggravates the problem. For, to the extent that the price to be paid for the shares is represented by undistributed income, a purchaser will be making a capital outlay which on liquidation will be taxed as income in his hands. If the purchaser is an individual, it will be taxed at personal rates. If the purchaser is an ordinary Canadian corporation, and often only a corporation will have sufficient funds to acquire another successful company, the worth to it of the undistributed income may be even more questionable. This is so because the undistributed income on hand, in the company to be acquired, at the beginning of the year in which its shares are sold becomes "designated surplus" and if distributed as a dividend will be taxed at ordinary corporate rates in the hands of the receiving corporation. Furthermore, if the balance is eventually received by individual shareholders it will be taxed again in their hands.

It is apparent then that the existence of a large earned surplus in a company may prove to be a serious problem when trying to negotiate a price for its shares, if the seller expects to sell the company's surplus for one hundred cents on the dollar. To avoid the problem posed by undistributed income and under-valued assets, a prospective purchaser will often seek to determine if it would be more advantageous to purchase the net assets of a company rather than its shares. Provided the amount of depreciation subject to recapture on the assets of the company to be acquired is not too substantial, it may well be that this will be the most sensible arrangement from the standpoint of a prospective purchaser. However, the owner of the private company is left with the problem of

the company's undistributed income. Fortunately, it can be distributed without it suffering too severe a tax impact, if the distribution is carefully planned.

For instance, the owner probably could arrange to liquidate the company through an investment dealer. The procedure is for him to sell his shares to the investment dealer for a price which would take into account the 20% tax which the company would be required to pay on dividends paid out of its designated surplus, and the dealer's fee for handling the transaction. As an alternative to this, the owner could liquidate the company over a period of years by having it pay dividends and elect to take advantage of section 105 of the Income Tax Act.

As far as a corporate purchaser is concerned the acquisition of control of a company with a large earned surplus is problem enough without having it taxed as ordinary income if received as a dividend. Occasionally, however, more by accident than design, there will be a ready-made solution to the designated surplus dilemma. This occurs where the shares of the company which is for sale are held by a personal corporation or an ordinary parent company without any retained earnings. In such a situation, the obvious tactic is to purchase the shares of the holding company instead of purchasing the shares of its subsidiary. It may be that, like children, companies should grow up with a parent in the background.

Where the owner of a private company builds up a successful business with the intention of leaving it to his heirs, the problems posed by the company's earned surplus may very well be of even greater importance than if he intended to sell the company. On his death, the shares of the company will be included in his estate. The value ascribed to the shares for succession duty purposes probably will not take into account the fact that the earned surplus will be taxable on distribution and the surplus may be dealt with as if it were invested capital. In addition to this, as so often happens, the company may have to declare a large dividend to pay the succession duties. Where this is necessary, the personal taxes payable on the dividends are apt to be substantial.

This problem has plagued a lot of estates and continues to imperil a great many more. Not infrequently, however, if recognized early enough, it can be solved quite satisfactorily. For instance, it is often possible to make good use of section 105 of the Income Tax Act and not just in respect of pre-1949 undistributed income. By systematically distributing dividends and electing to pay the 15% tax on an equivalent amount, in many cases it is possible to keep the earned surplus of a company within reasonable bounds. If need be, the funds received from a company in the form of dividends can be returned in the form of loans.

However, rather than wait for the trustees of his estate to effect the transfer of his company to his heirs under the terms of his will, the owner may find it to his advantage to start doing it during his lifetime. There are quite a number of courses of action which may be open to him, only one of which we will describe at this time.

Where the heirs of the owner of a company are employees, which term includes officers and directors, it is

possible for them to acquire a substantial interest in the company at a very modest cost to themselves by taking advantage of section 85A. All that is required is an agreement whereby the company agrees to issue shares of its common stock, apparently at any price, even if it is only nominal. The employee is deemed to receive a benefit equal to the difference between the value of the shares at the time he exercises the option and the price paid for the shares.

The employee may either include the benefit in his income and have it taxed as ordinary income or he may make an election to have the benefit taxed at a special rate. The special rate is his average rate of tax for the preceding three years, less 20 percentage points. The average rate of tax is determined by the ratio of total taxes (before credits for provincial and foreign taxes and dividends) to net income (income before personal exemptions, etc.). If the average rate is 19%, no tax will be payable and if it is 21%, the special tax is only 1%.

The employee is specifically required to make an election before he can take advantage of this section and, while he may complete his tax return using its provisions, he should file a formal letter of election at the same time.

From the above remarks it will be seen that in certain cases stock options may be used to accomplish a twofold purpose. They can be used to transfer part of an estate to the heirs at no cost or very little cost in income taxes while at the same time saving succession duties. Secondly, the problem of accumulated surplus is less severe in that dividends will be distributed to a larger number of persons who will pay less taxes on such dividends.

Attention is drawn to the fact that our remarks on stock options only touch upon one situation in which section 85A can be used to dilute an estate. The actual provisions of this section are quite broad and can be used to advantage in designing a stock purchase plan for employees to offer them a very worthwhile incentive.

It will be readily seen that it is quite possible to reduce potential tax liabilities buried in earned surplus if adequate plans are made in time. The above remarks suggest only a few of the possibilities but they all require forethought and planning. The owners of all companies which are not widely held cannot afford to overlook the fact that plans should be made early to alleviate the problems caused by the sale of the company or death of a principal shareholder, one of which events must ultimately occur.

BY JOHN W. CROWE, C.A.

Administrative Accounting

Accounting for Plant Stores

Methods specialists generally follow a ritual of asking such questions as "why, how, when, who, where"? The most fundamental of these questions is obviously "why". Yet it is the one question that systems experts often fail to pursue adequately.

A good example of this failure is in the field of inventory accounting. Most of us have been brought up with perpetual inventory records. Much effort and even ingenuity have been directed at determining the most efficient ways of recording a mass of details on perhaps thousands of inventory cards. The question "Is all the information necessary"? is seldom asked seriously. What purpose does it serve to have receipts and issues posted in minute detail? Is the purpose worth the cost?

In the case of plant mill supplies, maintenance stores and other low-priced inventories, it can be seriously debated whether detailed inventory records are in fact worth the cost. At an industrial plant there are hundreds, or even thousands, of these low-priced articles each normally accorded the dignity of a separate ledger card. While a relatively very large amount of effort is directed to recording and controlling these mill and maintenance supplies, such materials normally account for a small proportion of the total value of inventories on hand. Studies have shown that as high as 70% of the clerical effort in the stores and material control offices at some industrial plants goes to look after less than 15% of the total cost of plant inventories. Much more time is required to handle plant stores in the orthodox manner than is expended, for example, on raw materials and spare parts where there is probably real money invested.

What can be done about this problem? Instead of mechanizing or otherwise trying to speed up the processing of stores data, should we not attempt to eliminate or at least drastically reduce such processing?

For the purposes of this study let us define stores as the mass of lower-priced, usually fast-moving articles stocked at the average works, such as nuts, bolts, nails, electrical supplies, pipes, fittings, valves, cleaning materials, safety equipment and metal stock. At larger works we might add paints, lumber and insulating materials. The problem is to simplify as much as possible the accounting for these materials which may easily consist of thousands of items but amount in total to a relatively small sum of money.

One obvious answer which may well be workable at a small plant is to charge all purchases of such materials directly to costs. If we are worried about a distortion of inventory values this can usually be met by carrying forward as a constant figure the total value of these stores at the time of adoption of the new procedure. Periodically, say twice a year, this figure can be adjusted to an actual count.

Since there will be no detailed records, no time will be consumed in reconciling individual items of the count.

One might ask what about the matter of control? The materials can still be kept under lock and key and issued only to authorized individuals. At a small plant everything is quite closely under the scrutiny and control of the works manager. The manager is aware of current demands for maintenance supplies and probably approves all purchase orders. As for pilferage, the gate will still be guarded, and there is little evidence that detailed store records actually diminish the incidence of petty thefts. In any case, the cost of controls must be weighed against the cost of probable losses which the controls are designed to prevent. For example, from the viewpoint of possible loss it would be impossible to justify having, say, five people account for a stores movement of $50,000 a year. Yet such a staff can easily be engaged in posting and reconciling detailed perpetual inventory cards if there are thousands of items.

For a larger works, a system more refined than simply charging purchases to operations may be needed. The following approach which involves a bare minimum of accounting has been found to be highly workable in practice.

The stores are divided into a few broad classes such as:

1. Hardware and safety supplies
2. Lumber and insulating materials
3. Paints
4. Metal stock
5. Electrical supplies
6. Pipes, valves, fittings, etc.

Accounts are set up in the works ledger showing the opening inventories (at date of adoption of this system) in each class and so far as possible the stores are physically segregated by these classes. Detailed ledger cards accounting for the stores by individual items are forthwith discarded. What, if anything, do we have in their place?

In the physical stores area a card is attached to each bin for each item of stores. When incoming material is deposited in the bin the stock clerk posts on the bin card the quantity and unit price of the shipment received. When material is issued, *no* entry is made on the bin card. Requisitions, however, are still required for each issue and at the time of fulfilling each requisition the stock clerk notes on the requisition the latest unit price shown on the bin card. Filled requisition forms are kept in the stock room in piles by classes and periodically sent to the stores office.

In the stores office the requisitions are extended (using the price entered by the physical stock clerk) and credited in total to the appropriate class account. For the offsetting charge to expense the requisitions are resorted and summarized by cost accounts. Similarly, invoices for incoming material are sorted by and posted to the appropriate stores class account. The five or six class accounts therefore give a summary record of the cost only of receipts, issues and balance on hand.

Physical inventories of the stores are taken periodically, say, one class each month. Inventory sheets for a class are typed up in advance with the names of the items and latest prices taken from the bin cards. When the count of a class has been completed the stores office extends and totals the inventory sheets. The total count value

will, of course, differ from the balance in the ledger account for that class. The difference is reported to the works manager and automatically written off. No reconciliation is possible, but consistently large differences would call into question the efficiency of the stores supervisor and his staff. In practice, differences under this system have been found to be surprisingly insignificant. The key to any good stores control is not in accounting but in having a good supervisor in charge.

When the actual counts are being made quantities on hand and date are noted in an allotted space on the bin cards. With this information and the figures for quantities received previously noted on the card it is possible to calculate quickly the rate of turnover. From this, the stores supervisor or some other trained employee can estimate amounts for maximum and minimum stock. This information is also noted on the bin card and revised each time an actual count of the class is taken.

How is it known when the minimum stock has been reached and a new order should be placed? By visual inspection. To facilitate telling at a glance when re-ordering is needed, a number of schemes are possible. The minimum stock items can be segregated by a compartment within the bin, by using coloured lines, by cardboard dividers etc. When a stock clerk sees that re-ordering is necessary, he simply withdraws the bin card and sends it into the stores office. A red card underneath the bin card is left on the bin to signify that the stock clerk has started the ball rolling. The bin card should have a complete description of the stores item and may, perhaps, have a supplier's code. Since the quantity to be ordered should be the difference between maximum and minimum stock the typing of the purchase order can be done automatically and quickly from the bin card. The purchase order number is inserted on the bin card which is returned to the stock room.

One big job common to both this and the perpetual inventory system is the distribution of requisitions by cost codes. At large plants where all maintenance costs are accumulated by work orders this distribution can be particularly onerous. Here again a valuable short cut is possible. Studies at some plants have indicated that requisitions for amounts under $2 account for about 75% of the pieces of paper but only about 10% of the value of stores issued. Where this is the case, requisitions under $2 (or some other appropriate figure) can be safely eliminated from the cost distribution and charged in total to an overhead account. Seventy-five per cent of the distribution job is thereby eliminated.

The techniques outlined above normally result in a drastic reduction in clerical effort. Perhaps the most important problems in stores administration are those associated with re-ordering, maintaining minimum stocks and setting realistic maximums. In this sphere the system described for a larger plant has proved quite as efficient in practice as the perpetual inventory method. It involves a slight upgrading in the status of the physical stock clerks and gives the stores supervisor more freedom for active supervision in this area. This is undoubtedly beneficial since the efficiency and elimination of waste or loss in any stores depend more on what happens in the stock room than in the stores office. Differences between act-

ual costs and class control accounts are usually small. No detailed reconciliation is possible and the time usually consumed in this activity can be put to more fruitful purposes. It may appear anomalous to price both stores issues and inventory counts at the latest unit purchase prices. While the only defence is simplicity, the turnover of stores is usually fast and the change in prices relatively slow. Any distortion, therefore, of costs or inventory values will generally be insignificant.

Budgeting as an Effective Aid to Management

Budgeting is now recognized as one of the most effective aids to management. It is particularly effective when viewed as a basis for control over all phases of the operations of the business as well as a guide to future action. The design and operation of the budget requires the adoption of sound principles of (1) organization and utilization of personnel, (2) operational controls and (3) management reporting, to integrate and coordinate the efforts of practically every section of the business toward the attainment of overall management objectives. Today's concept of management embraces every level and area of authority in the company responsible for carrying out some part of the company's program. This includes not only the top executive group, but the successive levels of authority in sales, production, general administration and, in fact, any area of company operation where effective planning and control are required. A soundly conceived plan of budgetary control provides greater opportunities for the extension of the usefulness of the accounting function to all these levels.

A successful budget system must be based on a sound plan of organization in which each department and administrative group must understand the objectives of its particular activity and its relationship to the objectives of the company as a whole. Departmental relationships, lines of responsibility, and spheres of authority must be clearly defined and logically assigned. Fixing responsibility of specific individuals for efficient performance in accordance with the established plans is a fundamental concept of budgetary control. However, if specific individuals are to be held responsible for performance, they must know precisely what they are responsible for, and to whom. They must be vested with necessary authority, and clear-cut policies and procedures must be established to enable those accountable for performance to function properly. Failure to do this will cause departmental activities to get out of focus with overall company objectives and result in duplication or waste of effort.

The accountant's function is principally that of consulting with department heads in the course of preparing the budget, supplying them with essential data, coordinating departmental plans, integrating them with companywide objectives and presenting the complete budget to top management for approval.

—"Budgeting and the Corresponding Modernization of Accounting" by Joseph Pelej, C.P.A., *The Journal of Accountancy*, June 1958.

BY PETER C. BRIANT, M.B.A., C.A.

Current Reading

MAGAZINE ARTICLES

ACCOUNTING

"ACCOUNTING FOR A MUNICIPALLY OWNED TRANSIT SYSTEM," by John L. Williams. *Municipal Finance,* May 1958, pp. 136-140.

The current complexities of public transit financing emphasize the need for good records in a transit system. This article reviews the accounting procedures of the Phoenix, Arizona, public transit accounting system and includes brief historical references to stress the importance of good accounting and reporting.

AUDITING

"THE NATURE AND RELIABILITY OF AUDIT EVIDENCE," by R. K. Mautz. *The Journal of Accountancy,* May 1958, pp. 40-47.

How does an auditor know when he has acquired "sufficient evidential matter? How does one judge the "competence" of evidential matter? What is "evidential matter?" Do the various methods of acquiring evidence all provide evidence of equal validity?

After exploring these questions, Professor Mautz summarizes his ideas on the subject as follows:

1. Audit evidence includes any factual matter available to an auditor from which he may know or infer the relative truth or falsity of the assertions in financial statements.
2. Competent evidential matter includes:
   a) Real evidence — actual examination by the auditor of the thing in question — which is obtained by physical examination and count, recomputation, and retracing bookkeeping procedures.
   b) Testimonial evidence — oral or written statements by people — which is obtained by oral inquiry and written confirmation.
   c) Indirect evidence, i.e. documents, books and records, actions and events, and any other fact that the auditor uses in forming an opinion on financial statements. This evidence is provided by examination of authoritative documents, scanning, examination of subsidiary records, and correlation with related information.
3. The principal problems in dealing with audit evidence include:
   a) Obtaining sufficient competent evidential matter to afford a reasonable basis for an opinion.
   b) Screening and evaluating evidence. This includes the question of pertinence to the issue at hand, possibility of misinterpretation, and degree of conclusiveness for all types of audit evidence and certain other questions of reliability relating to sub-classes of audit evidence.

c) Reasoning from available evidence on the questions at issue. This is a simple matter if evidence on the issue is conclusive but a more difficult matter if the available evidence is inconclusive or judged unreliable.

4. Because of the great danger of drawing unwarranted inferences from audit evidence, the auditor must be extremely careful in his use of all evidence; his conclusions on every financial statement assertion should be related directly to the specific evidence on which it rests.
5. In the absence of conclusive evidence on any given issue, an auditor must rely on the most conclusive evidence available. When evidence sufficiently conclusive to support a judgment is not available, the auditor should refrain from making a judgment.
6. Because he alone collects, screens, evaluates, and uses evidential matter to determine the validity of assertions in the financial statements, the auditor must exercise special diligence in discharging his responsibility.

FINANCE

"Some Aspects of the Planning and Control of Capital Expenditure," by C. H. Brock. *Cost and Management*, May 1958, pp. 183-192

In this article, the eight basic phases of a planning and control program are discussed, and the author states what, in his opinion, are the principles on which any sound system for the control of capital expenditure planning should be based:

1. There should exist a long-term capital development plan towards which individual projects and short-term budgets must contribute, or with which they must be consistent.
2. Correct capital expenditure decisions and accurate control depend upon reliable pre-appraisal of of project cost and profitability which must take into account all financial aspects of the project, however they may be treated in the company's books. The recording of actual expenditure during construction, or post-completion studies, can never retrieve mistakes resulting from inadequate project preparation or of fallacious profitability measurement systems.
3. Capital expenditure control systems must be designed so that they will assist and not handicap management. They must concentrate management attention to the significant away from the unimportant and they must be capable of operation without the employment of a vast accounting staff.

PROFESSIONAL

"Challenge to Public Accounting" by Leonard Spacek. *Harvard Business Review*, May-June 1958, pp. 115-124.

This is a stirring challenge to the accounting profession in the United States to lean less on tradition for its authority and more on principles that are soundly related to current economic conditions. All economic groups, argues Leonard Spacek, must have an independent professional body to establish the accounting principles by which profits used in price and wage negotiation are determined. These groups may argue as to how the profits are to be distributed,

he writes, but what the profits *are* should not be subject to controversy.

Rejecting rigid regulation by a government agency, Mr. Spacek calls for the development of flexible standards for reporting costs and income so that uniform standards may be applied to all corporations in comparable conditions. Until objective standards of accounting are established, adopted by the profession, and explained to the public there will continue to be needless inconsistencies in financial reporting, warns the author, and corporate reports will continue to be suspect to all. We cannot risk public dissatisfaction, Mr. Spacek urges; for, when aroused, the public does extreme things, and becomes the dupe of those who would make men in government the sole arbiters.

Mr. Spacek lauds the action of the president of the American Institute of Certified Public Accountants (A.I.C.P.A.), who recently recommended the creation of a new research organization within that Institute to examine basic accounting assumptions and to develop authoritative statements of accounting principles, which, if approved by the Council of the Institute, would be considered binding on its members. This, in Mr. Spacek's view, may prove to be the first step by which the profession will meet its responsibilities to the public.

In this last respect, Mr. Spacek is not absolutely correct. It has always seemed to this reviewer that one of the strengths of the accounting profession in the United States has stemmed from the fact that while the A.I.C.P.A. has concerned itself with codifying current practice, the American Accounting Association (A.A.A.) has been actively engaged in the development of accounting principles on an *a priori* basis, a task for which, by virtue of its close ties with the universities, the A.A.A. is particularly well equipped. Admittedly, its "Statements" have been few in number and have not received the attention from accounting practitioners that they deserve. But they do represent an early attempt "to examine basic accounting assumptions and to develop authoritative accounting principles for the guidance of industry and the accounting profession. . . ." Now that the A.I.C.P.A. is entering into the field of the theorist, the interplay of ideas between the two groups may not be as lively as heretofore.

TAXATION

"Double Taxation of Corporate Earnings." *The Controller*, June 1958, pp. 280-281.

The Controller reports on a study of double taxation of corporate earnings conducted by Dr. Daniel M. Holland of the National Bureau of Economic Research. The purpose of the study is to show how heavy the alleged overtaxation or undertaxation is, what factors determine its size, and how it affects federal tax revenues in the years studied.

In his investigation, the author considers both distributed earnings and retained earnings as income allocable to the individual stockholder. Thus, both corporate and personal income taxes are treated as a stockholder's federal income tax liability. The combined tax is then compared with what the stockholder would pay if the rate schedule applicable to personal income were the only tax applied to this segment of his income. An excess of the actual tax paid over the liability in the hypothetical case

indicates that the stockholder is being overtaxed.

The following major conclusions of the study are reported:

1. Taxes paid by stockholders on earnings for distribution as dividends are substantially heavier than if computed according to personal income tax rates, but the extra burden is less severe at higher-income levels than at lower-income levels.
2. On retained earnings, the same general pattern follows, but the extra burden is less at all income levels. In top-income brackets there is marked undertaxation, mainly because the corporate income tax rate is less than the personal income tax rate in these brackets.
3. When both sets of earnings are combined as net corporate earnings, the extra tax differential again declines as stockholders are overtaxed when the component is analyzed, but wealthier stockholders are undertaxed by the present tax system.

BOOK REVIEWS

Cases and Materials on Income Tax, John G. MacDonald; Butterworth & Co. (Canada) Ltd., 1957; 695 pages; $18.50

The indefatigable John G. MacDonald has added this case book to his many important contributions to public knowledge in the field of Canadian income tax. From his experience both as a practising lawyer and a lecturer in taxation, he has selected, classified, arranged and reproduced the principal cases within the confines of a single volume.

The author states in his preface that, as this is primarily a student's book, it includes a few cases which have been reversed on appeal to a higher court so as to teach the student to approach his reading with a critical and enquiring mind and to consider carefully the reasoning that leads a judge to his decision before accepting it.

Except for the discussion notes at the conclusion of each chapter, most of the author's comments have been extracted from the service edited by him under the title of "Canadian Income Tax". In addition to the cases, many articles by other writers have been reproduced, including one written by this reviewer, who thus must confess that technically he is not in a position to express an independent opinion.

This book will be a very useful addition to the library of the practising accountant, notwithstanding that he already may have all the Canadian cases, as it includes many United Kingdom and Commonwealth judgments of importance in Canada not ordinarily available to him.

L. J. Smith, F.C.A.,
Toronto, Ontario

P

Sampling Techniques in Accounting, by Robert M. Trueblood and Richard M. Cyert; Prentice Hall, New York, pp xii, 211; $7.50

The application of statistical techniques to accounting and auditing is a subject which has been receiving a good deal of attention in certain quarters recently. However, it is probably fair to say that the great majority of accountants and auditors have done very little exploring in this area of their subject; this is not surprising in view of the apparent difficulty of the terrain and the lack of experienced guides. The situation

should now be improved by this publication, which might very well be termed a guide book on this subject, particularly since the authors have avoided cluttering the book with mathematical symbols and jargon.

The authors are eminently well qualified to write the book: Mr. Trueblood is a partner in the Pittsburgh office of Touche, Niven, Bailey and Smart and is chairman of a Committee of the American Institute of Certified Public Accountants set up to study the use of statistical methods by public accountants; Mr. Cyert is a Professor of Economics and a member of the American Statistical Association. The authors are both members of a small group of Pittsburgh statisticians and accountants who have been conducting research on the application of statistics to accounting and auditing for the past three or four years.

The book is divided into three sections. The first gives a general nontechnical review of statistical concepts, illustrated by data drawn from a sampling experiment with 59 accounts receivable ledgers. The second discusses the extent to which statistical methods are currently being applied in auditing practice and accounting and management control, sizes up the long-range prospects and suggests immediate courses of action. The third consists of nine case studies of statistical methods.

EDWARD STAMP, M.A., C.A.,
Toronto, Ontario

The Bank Audit, Bruce Marshall; Longmans, Green & Co., Toronto; 384 pages; $3.75

In literature, up to the present time, the chartered accountant has been rather neglected. When he does appear in a novel he is quite frequently cast as a sinister character or, if he is on the side of the angels, is inclined to be dull and dependable rather than dashing. Bruce Marshall, in his book "The Bank Audit", does much to redress this balance by creating not only a large cast of chartered accountants but also a plot which draws its main interest and suspense from the description of accounting practices.

Having reason to believe that a fraud is being successfully perpetrated on the Paris branch of an Anglo-French banking house, the auditors, a London firm of chartered accountants, alert their Paris staff to track it down. It is 1933, the depths of the depression in France and the staff of Messrs. Cloudridge, Parkinson, Talisman, Steeple & Co. have all taken salary cuts. Each man is anxious to be the one who discovers the fraud and thereby gains financial reward and possibly promotion. How the search sets them against one another and affects them all in their private and business lives makes a fascinating and intricate story.

Bruce Marshall was himself a chartered accountant and, at one time, worked in Paris. He manages to make the complicated business of accountancy a vital and interesting part of his story, building up the suspense until the eventual discovery of the fraud. This accurate, technical background is so expertly drawn that, while it makes the book of special interest to accountants, it is just as engrossing to other readers as well. The characters are a varied lot and thoroughly believable, and Mr. Marshall draws a lively and sometimes raffish picture of life in Paris on a small income.

R. E.

BY J. E. SMYTH, F.C.A.

Associate Professor, Queen's University

Students Department

PROBLEMS AND SOLUTIONS

Solutions presented in this section are prepared by qualified accountants and reflect the personal views and opinions of the various contributors. They are designed not as models for submission to the examiner but rather as such discussion and explanation of the problem as will make its study of benefit to the student. Discussion of solutions presented is cordially invited.

PROBLEM 1

Final Examination, October 1957

Auditing I, Question 1 (14 marks)

There are two types of events or transactions subsequent to the fiscal year end which require disclosure in the financial statements under review:

(i) Those that directly affect the accounts and financial statements of the client.

(ii) Those that do not affect the accounts directly but have to be considered in the interpretation of the financial statements.

Required:

(*4 marks*) (a) What would be a normal disclosure in the financial statements of the two types of subsequent events described above?

(*10 marks*) (b) List the procedures which CA should carry out in order to determine whether subsequent happenings have been properly reflected in the financial statements.

A SOLUTION

(a) **Normal disclosure of subsequent events**

If the events are of material significance and directly affect the accounts, the actual figures appearing in the financial statements should be adjusted.

If the events do not affect the accounts directly but are significant enough to merit consideration in interpreting the financial statements, they should be disclosed by means of notes to the financial statements.

(b) **Audit procedures to determine whether subsequent happenings have been properly reflected in the financial statements**

(1) Examine outstanding cheques and compare them with the cheque register to determine that the cheques were properly recorded and that none have been cancelled after the balance sheet date.

(2) Examine the larger cheques issued and cashed subsequent to the balance sheet date to determine that all liabilities of the previous period have been disclosed.
(3) Confirm accounts receivable balances and follow up any queries and payments to determine the collectibility of the accounts receivable shown on the balance sheet.
(4) Follow up contracts in progress at the balance sheet date to determine that the full liability for work completed at that date and the total commitment for the balance of the contract have been recorded or noted.
(5) Examine new contracts and purchase invoices subsequent to the balance sheet date to determine current market prices of the raw materials inventory.
(6) Compare inventory cost as reported on the balance sheet with current selling prices for the company's products to determine whether its normal rate of gross margin on sales will be maintained.
(7) Examine credit notes and receiving reports to determine that any significant subsequent returns which represent reversal of the sales of the previous period are properly recorded as such.
(8) Review the minutes of directors' meetings.
(9) Examine contracts and agreements entered into by the company including any signed after the balance sheet date.
(10) Review any interim financial statements or reports prepared for management which relate to the period after the balance sheet date.
(11) Discuss with management the subject of unusual or extraordinary happenings in the period after the balance sheet date.
(12) Re-examine market values of securities, materials, prices and foreign exchange rates in the period immediately after the balance sheet date and before the issue of the financial statements.
(13) Scrutinize the records for significant transactions recorded after the balance sheet date.
(14) Scrutinize capital expenditures made subsequent to the balance sheet date to disclose any extraordinary commitments which may have been made at that date.
(15) Check insurance policy cancellations subsequent to year end and other items which may affect prepaid expenses reported on the balance sheet.
(16) Examine income tax assessment notices.
(17) Scrutinize correspondence files.
(18) In the case of work in progress of a contractor, examine completed correspondence files to ascertain that all losses incurred subsequent to the year end have been provided for.

Editor's Comments

Bulletin No. 14 of the C.I.C.A. Committee on Accounting and Auditing Research includes the following recommendation among its "General Comments":

> "Because financial statements are generally issued some time after the close of the financial year, consideration should be given to the disclosure of any events subsequent to the date of the statements which may have a material effect on the financial position of the company or on its future prospects."

PROBLEM 2

Final Examination, October 1957

Accounting II, Question 6 (20 marks)

As at December 31, 1956 the balance sheet of H Co. Ltd. showed the following item among the assets:

Investment in and advances to associated companies – $805,000

In preparing the consolidated financial statements for inclusion in the annual report of H Co. Ltd. for the 1956 fiscal year, CA, the shareholders' auditor, finds that:

(*i*) The investment in and advances to associated companies is made up of the following, recorded at cost:

Common shares of S Co. Ltd., purchased January 1, 1955 – 2,400 shares		$260,000
Common shares of Y Co. Ltd., purchased January 1, 1956 – 1,050 shares		100,000
Bonds of S Co. Ltd., purchased January 1, 1956, par value $250,000, interest 4%		240,000
Advances and current accounts:	S Co. Ltd.	20,000
	T Co. Ltd.	85,000
	Y Co. Ltd.	100,000
		$805,000

(*ii*) On January 1, 1956, S Co. Ltd. purchased 2,000 shares of T Co. Ltd. for $290,000.

(*iii*) The capital stock of each of the companies has remained unchanged since 1950 and consists of the following:

	H Co. Ltd.	S Co. Ltd.	T Co. Ltd.	Y Co. Ltd.
5% preferred of a par value of $100 each	$250,000	$150,000	–	–
Common of a par value of $100 each	500,000	300,000	$240,000	$350,000

(*iv*) The surplus accounts for each of the companies for the last two years showed the following details:

	H Co. Ltd.	S Co. Ltd.	T Co. Ltd.	Y Co. Ltd.
Balance January 1, 1955	$526,750	$100,000	$ 73,000	$ 44,000
Add: Dividends received	24,000	–	–	–
Profit for 1955	100,000	150,000	14,000	5,000
	$650,750	$250,000	$ 87,000	$ 49,000
Less: Fixed assets adjustment (see (*v*) below)	–	$ 50,000	–	–
Dividends paid: preferred	$ 12,500	7,500	–	–
common	–	30,000	$ 12,000	$ 17,500
	$ 12,500	$ 87,500	$ 12,000	$ 17,500

	H Co. Ltd.	S Co. Ltd.	T Co. Ltd.	Y Co. Ltd.
Surplus December 31, 1955	$638,250	$162,500	$ 75,000	$ 31,500
Add: Dividends received	29,250	10,000	–	–
Profit for 1956	146,000	123,000	42,000	30,000
Transfer of balance of reserve for contengencies	–	–	15,000	–
	$813,500	$295,500	$132,000	$ 61,500
Less: Amortization of bond discount	–	$ 2,000	–	–
Dividends paid: preferred	$ 12,500	7,500	–	–
common	–	30,000	$ 12,000	$ 17,500
Surplus December 31, 1956	$801,000	$256,000	$120,000	$ 44,000

(*v*) The balance in the surplus account of S Co. Ltd. as at January 1, 1955, as set out above, was made up of:

Retained earnings	$47,000
Surplus on appraisal	50,000
Premium on issue of preferred shares	3,000

(*vi*) The item "Fixed assets adjustment", reflected in S Co. Ltd. surplus account, represents the reversal on January 31, 1955 of the balance of the appraisal surplus. The directors decided to adjust the value of the fixed assets to a cost basis of December 31, 1954 so as to agree with the tax department records.

(*vii*) The item "Amortization of bond discount", reflected in S Co. Ltd. surplus account, represents the annual write-off of the discount of $20,000 arising from the issue of $500,000 10-year bonds on January 1, 1956.

(*viii*) The item "Transfer of balance of reserve for contingencies", reflected in T Co. Ltd. surplus account, represents the reversal on December 31, 1956 of a reserve set up on December 31, 1954, which was no longer required.

(*ix*) During 1956, T Co. Ltd. commenced the manufacture of a product used by H Co. Ltd. in its production, and sales to H Co. Ltd. amounted to $125,000 during the year. These were sold at T Co. Ltd.'s regular mark-up of 25% over cost. As at December 31, 1956, H Co. Ltd.'s inventory included $20,000 of this item valued at cost to H Co. Ltd. An additional $5,000 worth had been received by H Co. Ltd. prior to the year end but was excluded from inventory as the invoice had been overlooked and not entered on the books.

(*x*) During 1956, S Co. Ltd. purchased a machine for $20,000 which it subsequently sold to H Co. Ltd. for $24,000. Because of the nature of the transaction, the profit on the sale was applied by S Co. Ltd. as a reduction of cost of goods sold. Depreciation thereon, in the amount of $2,400, was included by H Co. Ltd. in cost of goods sold.

Required:

Your calculation of the following balances which will be included in the consolidated balance sheet as at December 31, 1956:

(a) Earned surplus.
(b) Minority interest.
(c) Goodwill or negative goodwill on consolidation.

A SOLUTION

Balances Included in Consolidated Balance Sheet of H Co. Ltd.
as at December 31, 1956

(a) Surplus on consolidation				
Surplus of H Co. Ltd. per balance sheet				$801,000
Surplus of S Co. Ltd. per balance sheet			$256,000	
Add share of S Co. Ltd. in increase in surplus of T Co. Ltd. since acquisition:				
Surplus of T Co. Ltd. per balance sheet		$120,000		
Less				
Interest in surplus of T. Co. Ltd acquired by S. Co. Ltd. Jan. 1, 1956: 5/6 of ($75,000 + $15,000) =	$75,000			
Minority interest in T Co. Ltd. as at Dec. 31, 1956: 1/6 of $120,000	20,000			
		95,000		
			25,000	
Consolidated surplus S Co. Ltd.			281,000	
Deduct				
Interest in surplus of S Co. Ltd. acquired by H Co. Ltd. Jan. 1, 1955: 4/5 of ($100,000 – $50,000)		40,000		
Minority interest in consolidated surplus of S Co. Ltd. as at Dec. 31, 1956: 1/5 of $281,000		56,200		
			96,200	
Share of H Co. Ltd. in increase in surplus (consolidated) of S Co. Ltd. since acquisition				184,800
				985,800
Adjustments				
Add back portion of amortization of discount on bonds payable of S Co. Ltd. which applies to inter-company holdings: 1/2 of $2,000				1,000
				986,800
Deduct intercompany profit in inventories: 4/5 of 5/6 of 20% of ($20,000 + $5,000)			3,333	
Inter-company profit in sale of fixed assets: 4/5 of $4,000		3,200		
Less portion of elimination realized to date in depreciation		320		
			2,880	
				6,213
Consolidated surplus H Co. Ltd. at Dec. 31, 1956				$980,587

Note: Because the investment in Y Co. Ltd. is only 30%, it would be shown on the consolidated balance sheet of H Co. Ltd. as an investment in an associated company. Similarly, the advance to Y Co. Ltd. would be shown as an advance to an associated company.

(b) Minority interest

In S Co Ltd.			
5% preferred stock		$150,000	
Common stock – 1/5 of $300,000		60,000	
Consolidated surplus			
Surplus per books – ...... 1/5 of $256,000 =	$51,200		
Share of undistributed profit of T Co. Ltd. since acquisition: 1/5 of 5/6 of ($42,000–$12,000) =	5,000		
		56,200	
			$266,200
In T Co. Ltd.			
Common stock – 1/6 of $240,000		40,000	
Surplus – 1/6 of $120,000		20,000	
			60,000
Total minority interest			$326,200

(c) Goodwill on consolidation

Investment by H Co. Ltd. in S. Co. Ltd. Jan. 1, 1955		
Common stock – 4/5 of $300,000	$240,000	
Surplus – 4/5 of ($100,000 – $50,000)	40,000	
Equity acquired per books of S Co. Ltd.	280,000	
Cost of investment	260,000	
Negative goodwill		$ 20,000
Investment by S Co. Ltd. in T Co. Ltd. Jan. 1, 1956		
Common stock – 5/6 of $240,000	200,000	
Surplus – 5/6 of ($75,000 + $15,000)	75,000	
Equity acquired per books of T Co. Ltd.	275,000	
Cost of investment	290,000	
Goodwill		15,000
Negative goodwill on consolidation		$ 5,000

Editor's Comments

(1) Since part (a) of the question asks for the calculation of consolidated *earned* surplus, the first section of the solution to this part might better, in the editor's opinion, have excluded the $3,000 premium on shares (contributed surplus) on the accounts of S Co. Ltd. This part of the calculation would then have been as follows:

Earned surplus H Co. Ltd. Dec. 31, 1956			$801,000
Earned surplus S Co. Ltd. Dec. 31, 1956		$253,000	
Add increase in earned surplus of T Co. Ltd. (as shown in solution)		25,000	
		278,000	
Less Earned surplus of S Co. Ltd. acquired at Jan. 1, 1955 80% of $47,000	$37,600		
Minority interest in S Co. Ltd. at Dec. 31, 1956 — 20% of $278,000	55,600		
		93,200	
			184,800
Consolidated earned surplus H Co. Ltd. at Dec. 31, 1956 subject to adjustment for unrealized profit in inter-company transactions and bond discount			$985,800

(2) The solution to part (a) assumes (as is reasonable) that, in computing its interest revenue on bond investments, H Co. Ltd. has not amortized one-tenth of the discount relating to its investment in the bonds of S Co. Ltd. In other words, H Co. Ltd. records only interest revenue at 4% per annum on par value. The consolidating entries would be:

Dr. Bonds payable (S Co. Ltd.)	250,000	
Cr. Bond discount (S Co. Ltd.)		10,000
Cr. Bond investments (H Co. Ltd.)		240,000

To eliminate inter-company holding of bonds.

Dr. Bond discount	1,000	
Cr. Consolidated surplus		1,000

To eliminate the recorded amount of amortized bond discount which applies to inter-company holdings.

The figure for bond discount which would appear on the consolidated balance sheet as at December 31, 1956 would be $20,000 − $2,000 − $10,000 + $1,000 = $9,000, which is the amount of unamortized bond discount relating to the $250,000 bonds payable of S Co. Ltd. held by the public at December 31, 1956.

NEWS OF OUR MEMBERS

Alberta

James C. Miller, C.A. has been elected president of the Alberta Associated Chambers of Commerce and Agriculture.

British Columbia

W. R. Dunwell, C.A. announces the opening of an office for the practice of his profession at 27, 28 — 425 Howe St., Vancouver 1.

Reg. J. Forsyth, C.A. announces the opening of an office for the practice of his profession at 6274 Fraser St., Vancouver 15.

Cowan & Cowan, Chartered Accountants, announce the removal of their offices to 424 Burrard St., Vancouver 1.

Manitoba

Price, Waterhouse & Co., Chartered Accountants, and William Gray & Co., Chartered Accountants, announce that practice of their profession will be carried on jointly by the two firms, with offices on the 5th Floor, Canada Trust Bldg., Winnipeg.

J. A. Hillman, C.A. has been elected president of the Winnipeg Chapter, National Office Management Association.

Nova Scotia

A. Wm. Linton, C.A. and Howard A. MacKinley, C.A. announce the formation of a partnership for the practice of their profession under the firm name of A. W. Linton & Co., Chartered Accountants, with offices at Ste. 208, Canadian Pacific Bldg., Halifax.

Ontario

,F. L. Norwood, C.A. has been appointed treasurer of Supertest Petroleum Corp. Ltd., London.

Norman Rubinoff, C.A. announces the opening of an office for the practice of his profession at 1 St. Clair Ave. E., Toronto

George Baker, C.A. has been appointed secretary of The Rio Tinto Mining Co. of Canada Ltd., Toronto, and Donald A. Macfarlane, C.A. has been appointed treasurer of the group's operating companies.

J. F. Kidner, C.A. has been appointed treasurer of Canadian Oil Co.'s, Ltd., Toronto.

Joseph Sprackman, C.A. announces the removal of his office to 3296 Dufferin St., Toronto 19.

J. F. Vaughan, C.A., general manager, Port Weller Dry Docks Ltd., has been appointed a director of the company.

Quebec

Hyde & Houghton, Chartered Accountants, announce the removal of their offices to 233 Notre Dame St. W., Montreal 1.

J. Howard Gough, C.A. has been appointed treasurer of Canadian Aviation Electronics Ltd., Montreal, and C. D. Reekie, C.A. has been appointed comptroller.

West Indies

Peat, Marwick, Mitchell & Co., Chartered Accountants; Kemp, Birnie, Britchford & Co., Chartered Accountants; and Tapley, Bowman & Co., Chartered Accountants, announce the merger of their West Indies practices. Henceforth their practices will be conducted under the firm name of Peat, Marwick, Mitchell & Co., Chartered Accountants, with offices at Bay St. (P.O. Box 123), Nassau, Bahamas, and at 22-24 Duke St. (P.O. Box 76), Kingston and 2 Market St., Montego Bay, Jamaica.

INSTITUTE NOTES

B.C. INSTITUTE

53rd Annual Meeting: Changes of both locale and pace were features of the 53rd annual meeting of the B.C. Institute held on June 12 and 13, 1958 at Victoria, B.C. A committee of Victoria C.A.'s, headed by P. S. Watt, organized a varied and interesting program for the occasion. Highlight of the social events was a barbecue and dance held at the Grouse Nest, East Sooke.

At the June 12 afternoon technical session on "Key Economic Factors in Security Analysis", U.B.C. Professor Les Wong advised members to encourage directors of public companies to reveal total sales figures on financial statements. The government might at some time enforce the counterpart of S.E.C. regulations if many public companies persist in withholding important items for security analysis from financial statements.

Brenton S. Brown, prominent Vancouver insurance adviser, stated at the June 13 morning session that the failure of most insurance programs was one of assessment rather than execution. Accountants can give some assistance to clients by assessing the needs for insurance coverage.

At the June 13 members' luncheon, J. L. Helliwell, F.C.A., presented certificates of fellowship to A. Percy Foster and W. F. (Bill) Martin.

Officers for the 1958-59 year are George M. Miller, president; Frank E. Walden, vice-president; Peter Stanley, immediate past president.

Vancouver Students: The manager of the Vancouver division of the management controls department of Peat, Marwick, Mitchell & Co., Vernon G. Seadon, addressed the Students Society on "Providing Management Consulting Services for Audit Clerks" at a technical session luncheon on June 24, 1958.

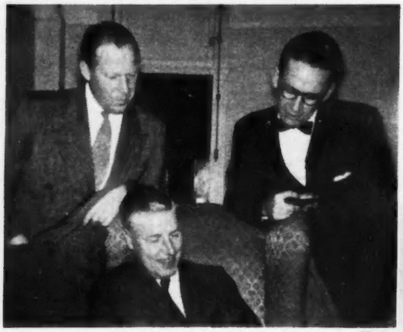
A North Vancouver ferry was chartered for an evening cruise on Burrard Inlet to celebrate the winding up of the 1958 season of the Students' Society Bowling League on July 5, 1958. The team from Collins and Collins led the league this year.

C.A. Club of Vancouver: The salmon fisheries v. hydro-electric power controversy was carried on at the meeting when A. Hans Swinton, solicitor and director of Moran Power Development Ltd., addressed the C.A. Club of Vancouver at the July 7 luncheon meeting.

ONTARIO INSTITUTE

1958 Annual Conference: Nearly 300 members of the Institute of Chartered Accountants of Ontario attended the Institute's third annual two-day conference, June 16 and 17. Held at the University of Western Ontario in London, the conference placed considerable emphasis on the non-accounting aspects of the C.A.'s overall interest in the problems of business.

The annual general meeting of members on Monday afternoon, June 16 was preceded by two sessions on "The Art of Administration" under the chairmanship of J. C. Taylor, F.C.A., Professor of Business Administration at the university. Interest in this topic was considerably heightened by the recommendation from a special subcommittee of the Provincial Institutes' Committee on Education and Examinations last year to the effect that the course of study leading to the C.A. certificate include some training in the principles and techniques of administration. The two sessions provided not only an excellent introduction to the subject but an opportunity for members to participate in several methods that have been used in helping people to acquire the art.



1958-59 B.C. INSTITUTE OFFICERS
***Left to right*: Peter Stanley, immediate past president; George Miller, president; Frank Walden, vice-president.**

Members of the Victoria planning committee review program of the meeting. *Standing, left to right*: Lloyd Jermain and Drummond Taylor. *Seated, left to right*: Gordon Green, Stewart Watt (chairman) and Dennis Roberts.

At the June 13 technical session, H. G. Craven and guest speaker, Brenton S. Brown, Vancouver insurance consultant.

AT THE GROUSE NEST, EAST SOOKE
P. Pedneault (*left*) explains the art of barbecuing salmon to Mrs. Peter Stanley, Mrs. F. A. McMenamin, F. A. McMenamin, president of the Oregon Society of Certified Public Accountants, Mrs. Bob McKean, Stewart Watt, Bob McKean and Peter Stanley.

ONTARIO EXECUTIVE 1958-59
Left to right: W. J. Ayers, Toronto, treasurer; R. B. Dale-Harris, Toronto, secretary; M. A. Bradshaw, Toronto, president; J. G. Brown, Kitchener, vice-president.

An informal reception followed the general meeting. F. W. P. Jones, dean of the University of Western Ontario School of Business Administration, was the guest speaker at the opening day dinner at which the new executive were presented to the members.

Dean Jones' address dealt with the importance of management's responsibility in profit-making, and the role of the accountant as a member of the only profession available to advise management in all its phases. True profit is a very long range proposition today, he said, as it must account for current costs; unpredictable expenses in the future, including expansion; unsuccessful business ventures; and expenses for charities, schools and hospitals. Over this long term, true profit is also very dependent on organized labour, the government and, naturally, the consumer.

"Because of this", said Dean Jones, "it is imperative that everything possible be done to make these three groups understand just what a true profit does for the economy of the country."

Profits are down today compared to 1950, he pointed out, and urged the members to help management examine its own profit potential. "Management may be missing many avenues open to restoring profits and the four routes that should receive particular emphasis are people, transportation, research and market development, and advertising.

Development of executives must be a continuing program, with no cessation during hard times. The eventual result of such cessation is a company of very old and very young executives, with nobody in between. Automation can carry us a long way, but real progress will still always be made only by people, he said.

Dean Jones showed the need for concentrated executive development by explaining that in 1933, as North America eased gently from the depression, one executive was needed for 25 employees, whereas today one is needed for eight employees. An important part in the encouragement of young executives is the stress placed on incentives by their companies, he said, and cited many examples of "incentive plans" now in effect with U.S. companies.

Regarding transportation, he remarked that most companies do 80% of their business with 20% of their lines. Most of them lose potential profit "by not always having the right lines at the right places at the right times".

"Nobody can afford to ignore research programs", he said and offered as an example the gold mining industry. This industry, in figuring its product must be good for "something other than Fort Knox and

Left to right: C. F. Gaviller, Owen Sound; O. C. Tidbury, Chatham; D. A. Sim, Ottawa; D. W. Burley, Niagara Falls.

human teeth", has a very elaborate research program to discover new uses for gold.

Advertising has become a major marketing power only since the war, he said, and many companies still misunderstand its uses. Good advertising "can be a real joy", but companies should decide carefully what they advertise and how.

At four concurrent sessions on Tuesday morning, June 17, the problems of public practice and matters of particular interest to members in industry were thoroughly explored. In an address titled "Sales Looks at Accounting", George F. R. Plummer, F.C.A. called for greater cooperation and understanding between comptrollers and

COFFEE BREAK
A group of Ontario members on the campus of the university.

sales managers or their counterparts. A panel discussion, chaired by D. Bruce Davis, F.C.A., brought out methods by which the practising firm can help the client through information obtained by the staff in the course of the audit. The pros and cons of the verification of inventories were discussed by a panel under the leadership of K. W. Lemon, F.C.A. while F. L. Norwood, C.A. delivered a paper, "Canada's National Accounts", which showed the available wealth of statistics and related material on future trends and conditions as they will affect particular businesses.

"Operations Research", a comparatively new and rapidly expanding facet of the Canadian business scene, was the subject of the conference's final plenary session, with R. A. McDougall, M.A. of Montreal as guest speaker.

M. A. Bradshaw was elected president for the year 1958-59 at the business session following the annual meeting. Other officers elected were: vice-president, J. G. Brown, Kitchener; secretary, R. B. Dale-Harris, Toronto; treasurer, W. J. Ayers, Toronto.

C. A. Scholarships: The Institute was pleased to note that B. S. Sutton, a winner of a C. A. scholarship in 1957, came first in first class honours in the Commerce and Finance course at the University of Toronto, in June 1958.

Affiliates: The following applicants have been admitted to membership by affiliation: V. A. Phillips (Que. '57), J. I. Spens (Scot. '14), E. Walton (Eng. '49), P. M. Watt (Eng. '57), J. S. Wilson (Scot. '26), H. Z. C. Chick (Inc. '55), C. V. B. Corbet (B.C. '47, Alta. '39), W. W. B. Dick (N.B. '47), R. Kettle (Eng. '50), G. O. Lind (Inc. '44), J. R. Neal (Sask. '50), D. D. Smith (Eng. '50), D. E. Wallis (Inc. '54), S. P. Wilkins (Eng. '44), R. A. Wilson (Alta. '56), W. S. Hulton (Scot. '49), D. J. Belton (Ire. '49), D. S. Butterfield (Que. '37, N.S. '53), C. M. Coulter (Eng. '57), K. P. Hayes (Que. 49).

QUEBEC INSTITUTE

The second annual conference, combined with the Institute's 78th annual meeting, was held at Laval University, Ste. Foy, (a suburb of Quebec City), on Monday and Tuesday, June 16 and 17.

Several hundred members gathered on Sunday, June 15 and were entertained at a reception at the university residence (Maison Biermans-Moraud).

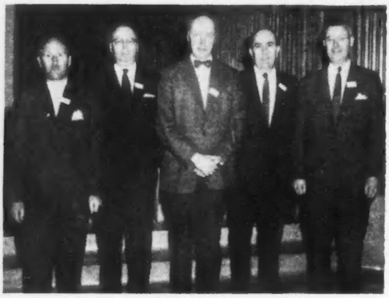
Sessions on Monday and Tuesday were held in the Faculty of Commerce building, half being conducted in French, half in English.

The lead-off session Monday morning, on the role of the chartered accountant in the changing economy, was divided into two panel meetings. The English meeting was under the chairmanship of Herbert Byleveld, economist of the Bathurst Power & Paper Co. Ltd., with W. Pierce Gould, R. M. Rennie and J. E. Smyth, associate professor of accounting at Queen's university,

as panelists. The French panel had Henri Ferron as chairman and J. J. St. Pierre, Jean Lanctôt and Marcel Bélanger as panelists.

The second morning session in English was on staff recruitment and training with G. Walter Brown of Brakeley Public Relations Ltd. as chairman and Julien Fayet, Norman LeBlanc and E. B. FitzRandolph as panel members. At the same time, two panel meetings were held in French, one on provincial income tax, with Lionel Roussin as chairman, Godfrey Gourdeau and Omer Pouliot as panelists, and the other on the gradual introduction of budgetary control, with Robert DeCoster as chairman, and Maurice Godbout and Gérard Larose on the panel.

The highlight of bilinguality was attained in simultaneous addresses Monday afternoon on the subject of professional



NEW QUEBEC EXECUTIVE
***Left to right*: Cecil Usher, secretary; C.-E. Belanger, treasurer; H. I. Ross, president; J. E. Maheu, 1st vice-president; M. L. Watt, 2nd vice-president.**

ethics, one in English by Rev. Brother Clément Lockquell, Dean of the Laval Faculty of Commerce, and the other in French by George P. Keeping, president of the Quebec Institute. The 78th annual meeting of the Institute also took place on Monday afternoon.

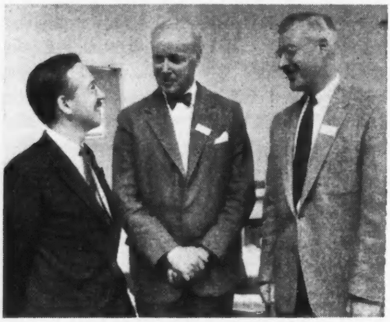
Discussion groups on Tuesday morning were as follows:

In English:

Elements of Cost—A. P. Smibert, chairman; Problems of Sole Proprietorships and Partnerships — W. I. Sheper, Henry Dobrin, (chairmen, 2 sessions); Inventory and Production Controls — F. V. Anderson, chairman; Audit Planning and Administration—Claude Allard and John F. Lewis, chairmen.

In French:

Professional Ethics—René Gagnon, Maurice DeCoster, (chairmen); Estate Planning —Paul Bruneau, chairman; Management Consultants—Marcel Caron, chairman.



AT THE QUEBEC CONFERENCE
***Left to right*: Albert Garneau, co-chairman of the Committee on Arrangements, chats with H. I. Ross and M. L. Watt.**

The committee in charge of arrangements for the conference consisted of Albert Garneau and K. P. Farmer, co-chairmen, Jules Bélanger, D. P. Cassidy, Maurice DeCoster, Godfrey Gourdeau, Marius Laliberté, Robert Noel, Gérard Renaud, Alphonse Riverin, Roger Roy, Roger-H. Stanton and Paul R. Thivierge.

NEWFOUNDLAND INSTITUTE

At a meeting on June 20, 1958 of the Institute of Chartered Accountants of Newfoundland, held in the Newfoundland Hotel, the following members were elected to serve on the Council of the Institute for the following year: president, E. M. Hunter; vice-president, F. D. Woolgar; secretary-treasurer, S. N. Inkpen; R. Leith, J. C. Newland, J. Hyslop, C. W. Earle, P. J. Gardiner and J. B. Marshall.

SAINT JOHN STUDENTS SOCIETY

The annual meeting of the society took place at the Admiral Beatty Hotel on

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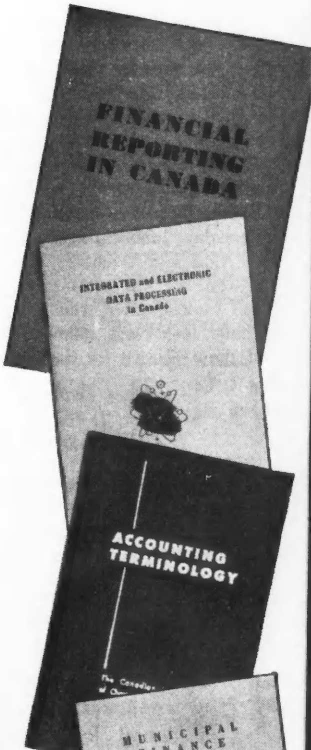

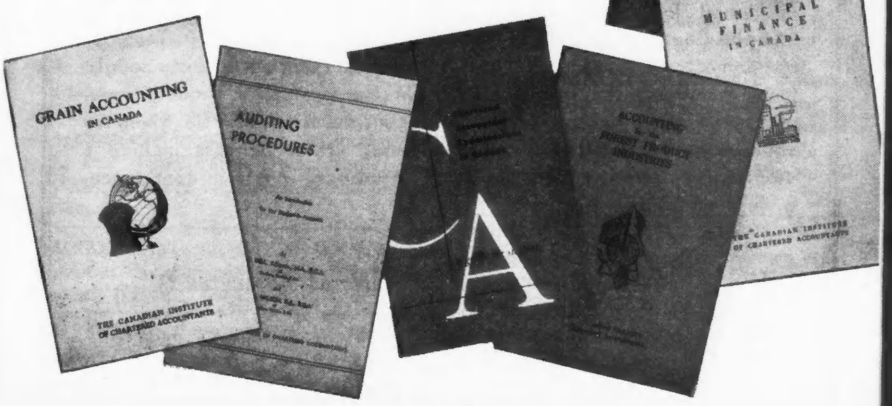

June 12, and the following officers were elected for the coming year: president, D. W. Buckle; vice-president, R. H. Hawkes; secretary, I. L. Currie; assistant secretary, D. E. Mowatt; treasurer, R. E. Campbell; executive members, A. J. Bourque, J. C. Bartlett, J. P. Michaud, H. A. Sharp.

On June 25 a social evening at the Renforth Community Club marked the end of the year's activities.

HAMILTON & DIST. STUDENTS

The annual meeting of the Hamilton and District Students Association was held on Thursday, June 26, 1958, at the Doon Valley Golf and Country Club, Preston. Approximately 130 members turned out on the golf course, after which the ninth annual dinner took place followed by the election of the executive for the coming year.

WINDSOR & DIST. STUDENTS

On Saturday, June 21, 1958, the Windsor students staged their version of a "Comedy of Errors". It consisted of a mixed (boys and girls) ball game at Point Pelee National Park. "A" team rallied in the final inning to edge "B" team 21 to 16. Following the game an auction was held. Each girl was asked to bring a picnic lunch for two and these various assortments were auctioned off to the men in the crowd.

On June 25, the branch held its second annual "Careers Night" at which the guests were students of Grades XII and XIII, interested in chartered accountancy, and their guidance teachers. Speakers of the evening were Kenneth Reid of the Department of National Revenue, William Copeland of Brokenshire, Scarff & Co., William McIvor of Kelsey Wheel Company and William Spencer of the students association.

The editor welcomes information for this column. News of members and provincial Institutes' activities received up to and including the 13th of the month will appear in the following issue of the journal.

CLASSIFIED ADVERTISEMENTS

All replies to box numbers should be sent to The Canadian Chartered Accountant, 69 Bloor Street East, Toronto 5, Ontario

Closing date is 13th of preceding month

THE NEW SOUTH WALES UNIVERSITY OF TECHNOLOGY — *Vacancy for Associate Professor of Accountancy.* The university invites applications for the position of associate professor in the school of accountancy. Salary £A2861 per annum. Applicants must possess a university degree and be members of a recognized professional accountancy Institute or Society.

The appointee will be responsible to the head of the school and will be expected to assist in the development of research programs and in the supervision of post-graduate students. The appointee will be eligible, subject to passing a medical examination, to contribute to the state superannuation fund for a pension of £A1400 per annum on retirement.

Associate professors are eligible for six months' study leave on full salary after three years of service or twelve months after six years of service. Subject to the consent of the university council, associate professors may engage in a limited amount of higher consultative practice.

The university reserves the right to fill the position by invitation. First-class ship fare to Sydney of appointee and his family will be paid.

Four copies of applications (including the names of three referees) and supporting documents should be lodged with the Agent General for New South Wales, 56 Strand, London, W.C.2, and a copy forwarded in an envelope marked 'University Appointment' by airmail to the Bursar, Box 1, Post Office, Kensington, New South Wales, Australia, not later than 31st August, 1958.

ACCOUNTING PRACTICE WANTED in Montreal by purchase or succession agreement. Box 766.

ACCOUNTING PRACTICE WANTED in Toronto by purchase or succession agreement by Western Canada firm. Box 798.

PRACTICE FOR SALE by chartered accountant, Edmonton and vicinity. Box 791.

JUNIOR PARTNER: Firm of chartered accountants with a nation-wide practice has an opening in its Montreal office for a junior partner. Generous salary for a one year trial period, to be followed by a definite arrangement for partnership if found suitable. Applicant should have had at least five year's experience in practice since obtaining C.A. degree. Replies will be treated as confidential. Qualified members of our staff have been advised of this advertisement. Apply Box 792.

RESIDENT MANAGER required by chartered account firm for branch office close to Vancouver. Reply, giving full particulars to Box 795.

SENIOR ACCOUNTANT REQUIRED by Western retail lumber company with head office in Winnipeg. Young chartered accountant with some experience in commercial field preferred. Position offers excellent salary and advancement to executive capacity. Applicants may write stating age and complete details of qualifications and experience to Box 797.

INTERMEDIATE STUDENT for office in Southern Ontario. Good opportunities for advancement. G. H. Ward, 6 Hayden St., Toronto 5. WA 1-1115.

STUDENT WANTED: Intermediate or senior by Greater Vancouver firm. Reply, giving full particulars to Box 796.

CHARTERED ACCOUNTANT, B.Com., age 32, married, 14 years experience in public accounting, industry and income taxes, seeks responsible position with industrial or commercial firm in Ontario or Quebec. Available September. Box 794.

YOUNG CHARTERED ACCOUNTANT available for part-time work, Toronto area, evenings and week-ends. Box 793.

C.A. age 35, desires supervisory position with public accounting firm in Toronto leading to partnership. 11 years public accounting experience. Top references. Box 799.

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